ACC Association of Corporate Counsel

Responding to Government Investigations

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The in-house bar association[SM]

Responding to Government Investigations

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The information contained in this InfoPAK[SM] was developed by the law firm of

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Introduction

In 2002, the United States Department of Justice formed a Corporate Fraud Task Force in order to concentrate its efforts at detecting, prosecuting and deterring corporate malfeasance. "[I]t is time to reaffirm the basic principles and rules that make capitalism work - truthful books and honest people, and well-enforced laws against fraud and corruption."

- President George W. Bush, announcing the Task Force's formation on July 9, 2002[2]

The mission given to this Task Force was to:

- Restore confidence to the marketplace;
- Provide fair and accurate information to the investing public;
- Reward shareholder and employee trust; and
- Protect the jobs and savings of hard-working Americans.

The government's emphasis on corporate investigations has led to a better working relationship between key investigative agencies, including, but not limited to,the Federal Bureau of Investigation, the Securities and Exchange Commission, the Internal Revenue Service and the Postal Inspection Service.

Also in 2002, Congress passed the Sarbanes-Oxley Corporate Fraud and Accountability Act, which strengthened the ability of federal prosecutors to seek enhanced criminal penalties for securities fraud, attempts to commit mail, wire, bank and health care fraud, certifying false financial statements, document destruction or tampering, and retaliating against whistleblowers. Since the inception of the Corporate Fraud Task Force, the Department of Justice has obtained over 500 corporate fraud convictions or guilty pleas, and charged more than 900 defendants and over 60 corporate CEOs and presidents with corporate fraud crimes in over 400 filed cases.

On February 18, 2004, United States Attorney General John Ashcroft spoke about corporate crimes. He stated "[w]hen inaccurate corporate reports mislead the many and enrich the few, a culture of greed contaminates our free and open markets….[C]orporate officers who deceive do not just violate the integrity of the marketplace….Corruption draws the business community into a web of deceit and graft, making them co-conspirators in picking the pockets of ordinary people. The unethical actions of corporate officers strangle innovation. Investors lose their savings. Employees lose their jobs. And the entrepreneurial spirit that drives economic growth is stunted because capital investment is less likely where there are doubts about a market's integrity."[3]

Criminal investigations are not the only investigative matters being conducted in the corporate setting. Increasingly, the Securities and Exchange Commission has become more- aggressive in routing out corporate misconduct. During fiscal year 2003, the SEC filed 199 financial fraud cases. From October 1, 2003 through June 21, 2004, the SEC filed an additional 350 enforcement actions, 72 of which involved financial fraud or reporting. There have been 32 instances where companies have been suspended from trading, and on 36 occassions the SEC has sought to freeze

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2 http://www.usdoj.gov/opa/pr/2004/July/04_dag_495.htm

3 http://www.usdoj.gov/ag/speeches/2004/agweb21804mo.htm

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assets against individuals and companies. In addition, the SEC has sought to bar 110 corporate executives and directors from serving in publicly traded companies.[4]

The federal government's investigations of corporate fraud are increasingly complex. For example, the combined resources of the Federal Bureau of Investigation, the Department of Health and Human Services and the Postal Inspection Service, supervised by federal prosecutors, set up a phony storefront operation in southern Illinois to investigate an alleged fraud against Medicare. This investigation, known as "Operation Headwaters" targeted medical device manufacturing companies and the fraudulent Medicare reimbursement advice they provided to their customers. This phony company, Southern Medical Inc., staffed by law enforcement agents and a cooperating witness, surreptitiously recorded telephone calls with health care providers, secretly videotaped meetings, and solicited bribes for Medicare officials in attempts to investigate corporate executives and their companies.[5] This investigation has led to indictments and to several large penalties assessed against companies, including a $600 million payment by a corporate target.[6]

This type of investigation is not unique in that corporate executives, who exercise great control over corporate activities, have become the primary targets for law enforcement agents. Along with the corporate entity, Chief Executive Officers, In-house General Counsel, Chief Financial Officers, Vice-Presidents, Reimbursement Directors and others have become the focus of investigations, often unbeknownst to the individuals until they have been secretly recorded on numerous occasions.

One need not read Department of Justice press releases to know that investigations into corporate malfeasance are on the increase. Every day, newspapers across the country emphasize this all to well. The general public is regularly inundated with media reports of Securities and Exchange Commission and grand jury investigations, indictments, trials and sentencing, collateral shareholder litigation, and corporate restatements of financial documents.

Responding to such investigations is not a luxury–it is a matter of corporate survival. Proper preparation is crucial before such an investigation is initiated, during the investigation and after the investigative process is completed. This InfoPAK will discuss the various types of investigations, the processes and techniques used during investigative inquiries, proper responses and defenses that should be considered, as well as the consequences associated with such investigations.

Section I of this InfoPAK provides a brief overview of the different types of governmental investigations that a corporation is likely to encounter.

Section II outlines relevant legal concepts and important government policies including: the theory of criminal liability for corporations; methods of proof concerning the element of knowledge regarding corporate activity; and relevant Department of Justice and Securities and Exchange Commission policies.

Section III sets forth various investigative methods utilized by investigative agencies in conducting corporate investigations. These methods include both covert techniques used when law enforcement does not want the corporation or its management to be aware that the investigation is ongoing, as well as those techniques that that are conducted in an overt manner.

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4 http://www.usdoj.gov/opa/pr/2004/July/04_dag_495.htm

5 *See United States v. Augustine Medical, Inc.*, Cr.# 03-321 ADM (D. Minn. 2004)

6 http://www.belleville.com/mld/belleville/5152035.htm;
http://medicalnewswire.com/artman/publish/article_747.shtml

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Section IV provides information regarding the duties and responsibilities of corporate management when it learns that an investigation is being conducted into activities conducted by the corporation or its agents.

Section V outlines various concerns and provides practical advice which is helpful when responding to a government investigation, including those considerations to be made when selecting the appropriate team or person to oversee the response, if any, to the investigation.

Section VI sets forth important information regarding the privileges maintained by corporations and how to protect such material from disclosure.

Section VII lists additional resources that can be accessed for a more in-depth analysis of the issues.

Section VIII incorporates a sample joint defense agreement and the Department of Justice's guidelines utilized in exercising its prosecutorial discretion regarding business entities.

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I. Types of Government Investigations

A. Criminal

Criminal charges are the most serious weapon in the arsenal of government investigators and prosecutors. Criminal investigations and their outcomes have the potential to be the most damaging aspect of misconduct allegations. Criminal investigations can devastate a company's financial reputation as well as that of its management and shareholders. Often, the damage is done regardless of the outcome.

Most criminal cases involving economic and regulatory offenses are brought only after law enforcement agents have extensively investigated allegations of wrongdoing. Some investigations last several years before charges are even filed. Many criminal investigations stem from allegations made by whistle blowers or disgruntled employees. These allegations present fruitful opportunities for investigators to utilize the grand jury investigative process for the purpose of furthering their inquiries.

The grand jury is a Constitutionally-mandated process in federal felony cases. The Fifth Amendment to the United States Constitution provides in part that "[n]o person shall be held to answer for a capital, or other infamous crime, unless on a presentment or indictment of a Grand Jury. . . ."[7] Federal grand jurors are selected at random just as jurors who serve in public courtrooms,[8] and the proceedings unfold behind a veil of secrecy.[9]

The authority of grand juries, however, is not limited to the formal initiation of charges. Grand juries are invaluable tools in criminal investigations.[10] The grand jury "can investigate merely on suspicion that the law is being violated, or even just because it wants assurance that it is not."[11] Counsel for grand jury targets and witnesses are not permitted to attend when the jury is in session; the prosecutor is the sole attorney authorized to present information and evidence to the grand jury.[12] Prosecutors are not required to present exculpatory evidence to a federal grand jury, because that body sits only to investigate and accuse, not to determine guilt or innocence.[13]

The compulsive power of the investigative grand jury is unmatched by any other legal proceeding. Grand juries are commonly utilized to obtain testimony from reluctant witnesses, secure more complete and truthful statements than otherwise are given by witnesses (otherwise known as "locking a witness in"), obtain documents (on occasion, by the truckload) without a showing of probable cause, force testimony even by witnesses who invoke their Fifth Amendment privilege against self-incrimination, keep targets "in the dark" about the matter, control public disclosure of the proceedings [how?], and deflect claims of improper motive or harassment.[14]

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[7] U. S. Const., Am 5.
[8] *See* 28 U.S.C.§§ 1861-1869.
[9] *See* Fed. R. Crim. P. 6(e).
[10] *United States v. R. Enterprises*, 498 U.S. 292, 297 (1991).
[11] *United States v. Morton Salt Co.*, 338 U.S. 632, 642-43 (1950).
[12] *See* Fed. R. Crim. P. 6(d)(1).
[13] *United States v. Williams*, 504 U.S. 36 (1992).
[14] *See generally,* Israel, Podgor & Borman, *White Collar Crime: Law and Practice*, pp. 295-301 (1996).

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Criminal investigations and charges lodged against individuals have been common place for two centuries. Within the last three years, however, criminal proceedings against corporations have become increasingly prevalent. Although there is no federal statute defining criminal liability for a corporation, Supreme Court case law has recognized, as early as 1909, that a corporation can be liable for violations of criminal law.[15]

Criminal investigations carry a sigma to corporations and management that rival the embarrassment of being charged. Business organizations find themselves embroiled in criminal investigations, whether as the target, subject or even the victim.[16] Due to the expanding role of criminal investigations in federal and state law enforcement and regulatory contexts,[17] corporate directors and officers should be prepared to confront and defend against criminal inquiries before they begin.

B. Civil

Business organizations and senior management commonly also commonly encounter civil investigations conducted by law enforcement agents and government attorneys. Unlike criminal inquiries that threaten the loss of liberty, civil matters seek monetary compensation, civil penalties, disgorgements, injunctive or declaratory relief. Civil investigations conducted by the SEC commonly result in specific court orders directed against continuing courses of conduct.[18]

Both state and federal agencies may initiate civil investigations relating to misconduct in the workplace. The Securities Exchange Commission, the Environmental Protection Agency, the Department of Health and Human Services, the Department of Agriculture, the Department of Labor and the state Attorney General's Office commonly hold primary responsibility for civil investigations.

Corporations that contract with the federal government regularly submit claims to agencies, including invoices and related documents. Submitting inaccurate information to the federal government is an invitation to investigations and lawsuits brought under the civil False Claims Act, which authorizes damage awards of up to three times the loss to the government.[19] The False Claims Act also provides protection to whistle blowers and *qui tam* plaintiffs, that is, those who bring suit on behalf of themselves and the United States for the purpose of receiving a share of the damages.[20] Based upon 1986 amendments to the False Claims Act, *qui tam* plaintiffs now may recover up to 25% of the damages paid by civil defendants, depending upon the extent to which the *qui tam* plaintiff "substantially contributed to the prosecution of the action. . . ."[21]

Agents compelling evidence and other information to support a civil case hold similar investigatory authority to agents investigating criminal cases. The grand jury, however, may not be used to investigate a matter that is solely civil in nature.[22] If information obtained in a grand jury proceeding

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15 *N. Y. Central & Hudson. R.R. v. United States*, 212 U.S. 481, 492-94 (1909).

16 Shapiro, S., *Thinking About White-Collar Crime: Matters of Conceptualization and Research* at 11 (1980).

17 *See, e.g.,* Sarbanes-Oxley Corporate Fraud and Accountability Act (2002).

18 *See* 15 U.S.C. § 78u(d) (SEC "may in its discretion bring an action . . . to enjoin such acts or practices. . .").

19 *See* 31 U.S.C. § 3729.

20 *See* 31 U.S.C. § 3730(h).

21 31 U.S.C. § 3730(d).

22 *United States v. Sells Engineering*, 463 U.S. 418, 431-33 (1983).

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subsequently becomes relevant to a civil matter, the evidence may be used in the civil case if disclosure is authorized by the district court upon a showing of particularized need.[23]

Civil investigators are able to obtain documents, subpoena testimony and interview individuals with knowledge of the case. In addition to these tools, the federal government authorizes civil investigative demands, most commonly to obtain documentary evidence. Civil investigative demands are enforced by the full power of the federal government[24], and often may be used in conjunction with criminal process during criminal federal grand jury investigations.[25]

C. Regulatory

Corporations and their management personnel may be subject to regulatory investigations as well. The Internal Revenue Service, the Food and Drug Administration, the Federal Deposit Insurance Corporation and other federal agencies each are empowered to investigate conduct within their respective purviews. Similarly, state and local government agencies conduct investigations. Each of these regulatory agencies has its own rules, investigative policies and statutorily created enforcement capabilities, including the authority to operate in conjunction with, or refer matters to, the Department of Justice for criminal inquiry. Each also has its own ability to obtain information from corporations concerning its investigation under circumstances that, upon default, are capable of forcing subpoenaed corporations out of business.[26]

The Fourth Amendment mandates that most law enforcement officers seeking to search a premises or location obtain a warrant. The warrant must be based upon "probable cause, supported by Oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized." Regulatory matters, however, often are investigated pursuant to specific enabling statutes, which are capable of authorizing warrantless inspections or searches pursuant to the "closely regulated industry" exception to the Fourth Amendment's warrant requirement.[27]

The Food and Drug Administration utilizes warrantless procedures to gain access to business premises based upon nothing more than written notice and the presentation of credentials.[28] Failure to comply with a FDA request for inspection may subject one to criminal prosecution.[29] Similarly, the public interest in monitoring and inspecting commercial premises for fire and safety

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23 *See* Fed. R. Crim. P. 6(e).

24 *See United States v. Witmer*, 835 F. Supp. 208, 211 (M.D. Pa. 1993); *United States v. Markwood*, 48 F.3d 969 (6th Cir. 1995).

25 *Witner*, 835 F. Supp. 208 at 218 (False Claims Act Civil Investigative Demand regarding wrongful procurement by Army appropriate notwithstanding criminal grand jury investigation regarding the same conduct).

26 *See, e.g.,* 26 U.S.C. §§ 7602 (IRS authority to examine books and records), 7604 (enforcement of IRS summonses), and 6103(h) (authority to refer to Department of Justice). *See also* 15 U.S.C. §§ 77a et seq. and 78a et seq. (SEC authority to investigate with view to both civil and criminal enforcement); *United States v. Aero-Mayflower Transit Co.*, 831 F.2d 1142 (D.C. Cir. 1987) (subpoena authority of Inspector General of Department of Defense); *Donovon v. Spaeda*, 757 F.2d 74 (3d Cir. 1985) (Department of Labor subpoena).

27 *See Colonnade Catering Corp. v. United States*, 397 U.S. 72, 77 (1970) (liquor industry "long subject to close supervision and inspection. . ."); *United States v. Biswell*, 406 U.S. 311 (1972) (Gun Control Act); *Crosby v. Paulk*, 187 F.3d 1339, 1346-48 (11th Cir. 1999) (nightclub part of "closely regulated industry"); *Winters v. Bd. of County Commissioners*, 4 F.3d 848, 852 (10th Cir. 1993) (pawnshops).

28 21 U.S.C. § 374.

29 21 U.S.C. § 331(f), 333(a).

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compliance may validate a warrantless search, provided the enabling statute or administrative regulation articulates reasonable standards with respect to a particular type of building and the search is not implemented for the purpose of undertaking a criminal investigation.[30]

D. Parallel

Parallel proceedings exist "when two or more investigations or actions, concerning allegations arising from the same (or substantially the same) set of facts, proceed simultaneously or successively against the same or related parties."[31] Criminal, civil, and administrative investigators will often coordinate combined strategies, resources and investigative tools in order to maximize their collective impact on a corporation. This coordination must address the merits of the respective matters, sensitivity to grand jury secrecy requirements, concerns regarding revealing confidential investigative techniques, discovery obligations, statutes of limitations and the potential consequences available.[32]

All federal prosecutors' offices have been directed to coordinate the criminal, civil and administrative aspects of all white-collar crime matters that arise within their jurisdictions. This includes: (1) timely assessment of the civil and administrative potential in all criminal case referrals, indictments, and declinations; (2) timely assessment of the criminal potential in all civil case referrals and complaints; (3) effective and timely communication with responsive agency officials, including suspension and debarment authorities, to enable agencies to pursue available remedies; (4) early and regular communication between civil and criminal attorneys regarding *qui tam* and other civil referrals, especially when the civil case is developing ahead of the criminal prosecution; and (5) coordination, when appropriate, with state and local authorities.[33]

Parallel proceedings commonly present the subjects of an investigation with a Constitutionally permissible "Hobson's Choice." The record developed during civil litigation may provide investigators, prosecutors and even juries handling a criminal matter with evidence that, in the absence of civil litigation, would have been unavailable in the criminal case. Subjects and targets commonly are forced to choose whether to testify in the civil matter (and create a record of statements to be used against themselves in the criminal case), or invoke a Fifth Amendment privilege against self-incrimination in the civil case in order to protect the criminal matter, only to have decision to remain silent used against the subject in the civil case for the purpose of drawing an adverse inference. To alleviate the "Hobson's Choice," district courts will entertain motions to stay civil litigation pending completion of the criminal trial, in particular when a defendant has already been charged.[34]

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[30] *See Camera v. Municipal Court of City and County of San Francisco*, 387 U.S. 523 (1967); *See v. City of Seattle*, 387 U.S. 541 (1967).

[31] Practicing Law Institute, Parallel Proceedings §IA

[32] United States Attorney's Manual, Chapter 1-12.00 (Parallel Proceedings), Organization and Functions Manual at 27.

[33] *Id.*

[34] *See Sterling Nat'l. Bank v. A-1 Hotels Int'l.,* 175 F. Supp. 2d 573, 575-76 (S.D.N.Y. 2001).

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II. Relevant Legal Concepts and Governmental Policies

It is crucial to understand the relevant legal concepts and the policies of any governmental agency that has authority to investigate a corporate entity. Each agency has its own methods of investigation, determines its own priorities for enforcement and resolves matters in differing ways. However, there are certain overriding issues that face most corporations today and that transcend industries. Accordingly, this section of the InfoPAK sets forth issues and principles that are most relevant in the current legal environment.

A. Elements of Corporate Criminal Liability

Corporations, while legal entities, act only through their agents (*i.e.* directors, officers and employees). An agent of the corporation who commits crimes within the context of his or her employment subjects the corporation to potential criminal charges by law enforcement authorities. As many corporations currently employ thousands of individuals, the number of employees magnifies the risk to the corporations. The following three elements must be met to subject a corporation to criminal liability:

- Each essential element of the crime charged against the corporation must have been committed by one or more of its agents;
- In committing those acts, the agent(s) must have intended, at least in part, to benefit the corporation; and
- The act must have been within the scope of employment of the agent who committed it.[35]

1. Practical Application of Corporate Liability

While a strong compliance program is essential–as are strong policies and procedures for corporations–if an agent of a corporation acts within the scope of his employment, the fact that such act was illegal, contrary to his employer's instructions or even against the corporation's policies often will not relieve the corporation of responsibility for that act.[36] "The foregoing is a simple conclusion inherent in a complex concept. A corporation which employs an agent in a responsible position cannot say that the man was only 'authorized' to act legally and the corporation will not answer for his violations of law which inure to the corporation's benefit."[37] Additionally, even if the original act was not within the scope of the agent's employment, but the corporation later approved or "ratified" the act though another agent who had full knowledge of the act and who was acting within the scope of his employment, then the corporation also may be criminally liable.[38]

The activities falling within the scope of employment generally are those that: (1) the employee is employed to perform; (2) occur substantially within the authorized limits of time and space; and (3) are actuated, at least in part, by a purpose to benefit the corporation.[39] The review of facts as they

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[35] *See* Eighth Circuit Manual of Model Jury Instructions, § 5.03 (2003).

[36] *See United States v. Hilton Hotels Corp.*, 467 F.2d 1000, 1004 (9th Cir. 1972).

[37] *Continental Baking Co. v. United States*, 281 F.2d 137, 150 (6th Cir. 1960).

[38] *Id.* at 149.

[39] *United States v. Gold*, 743 F.2d 800, 823 (11th Cir. 1984).

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relate to the element of "benefit to the corporation" generally does not provide a defense for the corporation. If the corporate agent intended to benefit the corporation when committing his crime, it does not matter that the actions ultimately provided little or no benefit to the corporation.[40] Nor does it matter that the agent's actions ultimately benefited himself.[41]

2. Collective Knowledge

The doctrine of "collective knowledge" provides that the requisite mental state or knowledge of the corporation need not be held by a single individual, but instead may be established by imputing to the corporation the "collective knowledge" of all the individuals involved in the action.[42] This theory of imputing criminal knowledge to a corporation arises from how corporations conduct their business.

> Corporations compartmentalize knowledge subdividing the elements of specific duties and operations into smaller components. The aggregate of those components constitutes the corporation's knowledge of a particular operation. It is irrelevant whether employees administering one component of an operation know the specific activities of employees administering another aspect of the operation.[43]

Accordingly, as corporations routinely operate their day-to-day activities through collective knowledge, corporations are increasingly exposed to liability under the theory of imputed collective knowledge.

3. Responsible Corporate Officer Doctrine

Generally, directors and officers of a corporation are criminally liable only if they actively participate in, conspire to commit, or aid and abet in committing a crime.[44] However, there are offenses that that have lead to the "Responsible Corporate Officer Doctrine." Courts have held that a corporate officer falls within this doctrine provided the officer had authority to exercise control over the corporation's activity that led to the offense.[45]

The Responsible Corporate Officer Doctrine arose originally in cases involving the Federal Food, Drug and Cosmetic Act, legislation enacted to provide guidance in a highly regulated area.[46] Because crimes under the Act were strict liability offenses, corporate officers faced personal criminal liability for offenses, even though they may not have known about the alleged wrongful conduct. Similarly, in the highly-regulated environmental context, "responsible corporate officers" fall within the definition of "persons" subject to prosecution for criminal offenses.[47] However, while prosecutors have this doctrine in their arsenal, courts have expressed a reluctance to hold corporate

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40 *Id.*

41 *Id.*

42 *United States v. Bank of New England, NA,* 821 F.2d 844, 856 (1st Cir. 1987).

43 *Id.*

44 *See, e.g., United States v. Amrep Corp.*, 560 F.2d 539 (2nd Cir. 1977).

45 *United States v. Iverson*, 162 F.3d 1015 (9th Cir. 1998).

46 *United States v. Dotterweich*, 320 U.S. 277 (1943); *United States v. Park*, 421 U.S. 658 (1975).

47 33 U.S.C., § 1319 (c) (6) (Clean Water Act); 42 U.S.C. § 6901 *et seq*. (Resource Conservation and Recovery Act (RCRA)).

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officers criminally responsible where knowledge of the offenses is presumed only through their position as a corporate officer.[48]

B. Control Person Liability

Much like the criminal theory of liability espoused in the "Responsible Corporate Officer Doctrine," in the civil securities field the doctrine of "Control Person" liability must be considered. The Securities Exchange Act of 1934 provides:

> Every person who, directly or indirectly controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.[49]

Accordingly, this control person liability allows for derivative liability in securities litigation, absent a showing of good faith. This defense of good faith is an affirmative defense, which will be successful if it is shown that there was no reckless act and that reasonable care was used to prevent any securities violation.[50]

C. Relevant Department of Justice Policies

1. Thompson Memorandum

On January 20, 2003, the Department of Justice ("DOJ") issued a memorandum addressing federal prosecution of business organizations.[51] This document is commonly referred to as the Thompson Memorandum and is a revision to the Holder Memorandum, which dates to 1999.

The Thompson Memorandum sets forth principles to guide federal prosecutors in their decisions whether to seek charges against a business organization. The Thompson Memorandum discusses a number of factors that DOJ and Assistant United States Attorneys should consider in determining whether to prosecute a business organization. These factors include:

- The nature and seriousness of the offense;
- The pervasiveness of wrongdoing within the corporation;
- The corporation's history of similar conduct;
- The corporation's timely and voluntary disclosure of its wrongdoing and its willingness to cooperate in the investigation of its agents, *including, if necessary, the waiver of corporate attorney-client and work product protection*;
- The existence and adequacy of the corporation's compliance program;

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48 *United States v. MacDonald & Watson Waste Oil Co.*, 933 F.2d 35 (1st Cir. 1991).

49 15 U.S.C. § 78t(a).

50 *Dellastatious v. Williams*, 242 F.3d 191, 194-95 (4th Cir. 2001).

51 http://www.usdoj.gov/usao/eousa/foia_reading_room/usam/title9/crm00161.htm

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- The corporation's remedial actions, including efforts to implement an effective corporate compliance program and cooperate with relevant government agencies;
- Collateral consequences, including harm to shareholders and impact upon the public arising from the prosecution;
- The adequacy of the prosecution of individuals responsible for the corporation's malfeasance; and
- The adequacy of remedies such as civil or regulatory enforcement actions.

In discussing the adequacy of a corporation's cooperation, the Thompson Memorandum specifically provides that prosecutors are permitted to consider whether a corporation waived the attorney-client privilege and the work product doctrine in determining whether to charge, and if so, which offenses to charge.

> One factor the prosecutor may weigh in assessing the adequacy of a corporation's cooperation is the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protections, both with respect to its internal investigation and with respect to communications between specific officers, directors and employees and counsel.

While the Thompson Memorandum makes clear that DOJ does not consider the waiver an "absolute requirement," it describes these waivers as "often critical" to the government's evaluation of the completeness of a corporation's voluntary disclosure and cooperation.

In this respect, the Thompson Memorandum indicates that the waiver normally should be limited to the "factual internal investigation and any contemporaneous advice given to the corporation concerning the conduct at issue." And, "[e]xcept in unusual circumstances, prosecutors should not seek a waiver with respect to communications and work product related to advice concerning the government's criminal investigation." While corporations can take some comfort in the fact that the government's request may be limited in scope during its investigation or that the government and the corporation may agree with one another that the waiver is limited to the government, a waiver by the corporation may cause third parties to seek and obtain materials disclosed to government investigators. See Section VI. E. 1. a. (Limited Waivers).

2. Ashcroft Directive

On September 22, 2003, in a speech in Milwaukee, Wisconsin, Attorney General John Ashcroft announced that he was issuing a new directive to federal prosecutors. He stated that this directive was going to be "direct and emphatic." This directive is set forth below.

> It is the policy of the Department of Justice that federal prosecutors must charge and pursue the most serious, readily provable offense or offenses that are supported by the facts of the case except in limited, narrow circumstances. In virtually all cases, prosecutors must bring the toughest charges available, yielding the toughest penalties under the sentencing guidelines.[52]

[52] http://www.usdoj.gov/ag/speeches/2003/092203milwaukee.htm

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This directive currently is being implemented on a routine basis in negotiating potential offenses that a prosecutor will consider in plea-bargaining, whether involving an individual or a corporation.

3. Practical Effects of These Policies on Corporations

These two Department of Justice policies have a profound impact on how a corporation should respond when faced with a government investigation. Under the *Ashcroft Directive*, federal prosecutors will be searching for the most serious offenses to investigate and potentially prosecute. Thus, this directive has significantly affected the process of "charge bargaining," under which defense counsel negotiates with the prosecutor regarding which charge and how many charges will be presented to the grand jury. The prosecutors are now limited by this directive and the corporation generally must face the most serious relevant offense. Charge bargaining to eliminate potential serious offenses has tremendous benefits to a corporation under investigation. The ultimate impact on the corporation can change drastically depending upon the offense(s) selected for prosecution. Additionally, the opinions of the corporation held by senior management, shareholders and the public will be profoundly influenced by the specific offenses charged.

The *Ashcroft Directive* potentially has severe consequences for corporations in certain industries. A health care provider, for example, may suffer collateral consequences associated with certain criminal offenses that essentially may drive the corporation out of business. If a corporation in the health care industry is investigated for conduct undertaken by its employees, and the Department of Justice charges and seeks as part of any settlement a guilty plea to the "most serious, readily provable offense," the corporation would likely be subject to mandatory exclusion from participating in federal health care programs.[53] This exclusion could, in and of itself, result in the corporate "death penalty"–that is, a complete collapse of the corporation's viability as a business.

The Thompson Memorandum has focused federal prosecutors upon the potential availability of obtaining internal investigations and has given them added ammunition to have internal investigations released. The fourth principle enumerated in the memorandum states that one consideration which DOJ may weigh when determining whether to bring charges against the corporation is whether there has been a "timely and voluntary disclosure of its wrongdoing." Internal investigations often are a ready source of information regarding the activities that are subject of the government's investigation. Additionally, however, DOJ evaluates the corporation's "willingness to cooperate in the investigation." This factor is often interpreted as the corporation's willingness to share the results of its internal investigation, even if it requires waiving privileges.

The waiver of privileges and the disclosure to DOJ of the results of an internal investigation may positively affect the decision whether to seek criminal charges. However, disclosing the results of the internal investigation also may provide all the necessary information to allow the government to bring criminal charges against the corporation or its individual employees. Additionally, as discussed later, this disclosure to the DOJ likely will result in the discoverability of the report to third parties. See Section VI. E.1.a., infra.

Accordingly, if the allegations are serious, and in the nature of potential federal criminal violations, these DOJ policies must be considered and their potential impact accounted for as early as the initiation of the internal investigation.

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[53] *See* 42 U.S.C. § 1320a-7.

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D. United States Sentencing Guidelines

In 1984 the United States Congress radically altered the federal sentencing process. With The Sentencing Reform Act of 1984, Congress sought to develop guidelines that would "further the basic purposes of criminal punishment: deterrence, incapacitation, just punishment and rehabilitation."[54] The objective of implementing the United States Sentencing Guidelines (hereinafter the "Guidelines") was "to enhance the ability of the criminal justice system to combat crime through an effective, fair sentencing system."[55] Congress sought to achieve this objective by creating a system that sought: (1) honesty in sentencing, (2) reasonable uniformity, and (3) appropriate proportionality.[56]

In 1991, the Organizational Sentencing Guidelines were adopted, creating a more uniform sentencing process for business organizations. These organizational guidelines "provide for penalties that equal or often massively exceed those previously imposed on corporations."[57] "The Guidelines offer powerful incentives for corporations today to implement compliance programs to detect violations of law, promptly …report violations to appropriate public officials when discovered, and … take voluntary remedial efforts."[58]

The Guidelines include a chapter devoted specifically to punishing organizational defendants. Organizations are defined as "a person other than an individual."[59] This term includes corporations, partnerships, associations, joint-stock companies, unions, trusts, pension funds, unincorporated organizations, governments, political subdivisions and non-profit organizations.[60] Chapter 8 of the Sentencing Guidelines provides specific direction to judges regarding how to calculate the sentence of a corporation that ultimately is adjudicated guilty of a criminal offense.

U.S.S.G.§8C2.5 is highly relevant to this InfoPAK–it sets forth the process for the court to determine the "culpability score" for the organization, which affects the potential sentence that the judge can impose. A corporation's culpability score is improved when it cooperates in a "timely and thorough" fashion.[61] According to the Organizational Sentencing Guidelines, this cooperation, to be considered in its most favorable form, must begin essentially when the organization is notified of the criminal investigation and should include the disclosure of all pertinent information known by the organization.[62]

Additionally, the Sarbanes-Oxley Act of 2002 was passed by Congress "to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant the securities laws." Sections 805(a) and 905(a) of Sarbanes-Oxley required the United States Sentencing Commission to review, and if appropriate, amend the guidelines to ensure that the serious nature of fraud offenses are recognized and sufficient penalties are in place to deter these offenses. As a result of this

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[54] Statutory Mission, United States Sentencing Guidelines, Chapter One, Part A 2.
[55] Policy Statement, United States Sentencing Guidelines, Chapter One, Part A 3.
[56] *Id.*
[57] *In re Caremark*, 698 A.2d at 969.
[58] *Id.*
[59] United States Sentencing Guidelines, Chapter Eight, Part A, § 8A1.1, application note 1. *See also* 18 U.S.C. § 18.
[60] *Id.*
[61] United States Sentencing Guidelines, Chapter Eight, Part A, § 8C2.5, application note 12.
[62] *Id.*

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Congressional directive, the Sentencing Commission amended the Guidelines to enhance penalties for offenses that commonly are uncovered in governmental investigations of public corporations.[63]

E. Relevant Securities and Exchange Commission Policies

1. "Seaboard Doctrine"

On October 23, 2001, the Securities and Exchange Commission issued a Statement on the Relationship of Cooperation to Agency Enforcement Decisions regarding a cease-and-desist proceeding against the former controller of a Seaboard Corporation subsidiary. This document articulates what commonly is referred to as the "Seaboard Doctrine."

The SEC explained that it decided not to take action against Seaboard Corporation for the conduct of its former employee "given the nature of the conduct and the company's responses." The SEC also provided a set of criteria that it "will consider in determining whether, and how much to credit self-policing, self-reporting, remediation and cooperation" in its investigations of corporations.

The criteria that the SEC has indicated it will take into account in determining the appropriate action to be taken against a corporation include:

- The nature of the conduct involved;
- How the misconduct arose, including whether compliance procedures were in place to prevent the misconduct;
- The level in the organization at which the misconduct occurred;
- The duration of the misconduct;
- The extent of harm caused by the misconduct;
- How and by whom the misconduct was detected;
- How long after the discovery of the misconduct it took for the company to implement an effective response;
- What the company did upon learning of the misconduct;
- What processes the company followed to resolve the issues and ferret out necessary information;
- Whether the company committed to learning the truth, fully and expeditiously;
- Whether the company promptly made available to the SEC staff the results of its review and provided the SEC with sufficient documentation of its response to the situation;
- What assurances there are that the conduct is unlikely to recur; and
- Whether the company has changed since the misconduct through merger or bankruptcy reorganization.

Accordingly, like the Department of Justice in making its determination regarding the appropriate action to take against a corporation, the SEC will consider whether the corporation conducted an internal investigation, the thoroughness of the investigation, the remedial actions, if any, that were

[63] United States Sentencing Guidelines, Chapter Two, § 2B1.1(b)(2)(c) and (b)(14).

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taken as a result of learning about misconduct allegations, and whether the corporation waived its privilege and released the results of the investigation to the SEC.

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III. Investigative Methods

The methods for investigating alleged corporate misconduct are limited only by the imaginations of the investigators. While regulatory investigations are likely to proceed in a fairly routine fashion, criminal investigatory techniques have expanded to include methods adapted from successful investigations into other areas of the law. It is no longer only organized crime and drug traffickers whose conversations are surreptitiously tape recorded, or whose meetings with an undercover agent posing as a business associate are monitored by law enforcement agents, or whose telephone and bank records are analyzed and their friends and neighbors are questioned. These same techniques are currently utilized to investigate corporate conduct by federal and state governmental agencies.

Investigative techniques generally consist of two broad categories: covert and overt. Covert investigations, as referred to in this InfoPAK, are those that are conducted by law enforcement agencies in such a manner as to preclude the target of the investigation from knowing they are under investigation. Overt investigations, on the other hand, are undertaken by law enforcement agents with the realization that the target of the investigation either will, or is likely to, become aware of the nature of the investigation.

A. Covert

Covert investigative techniques have become more prevalent in the area of corporate and white collar investigations. These techniques allow the law enforcement agencies to gather evidence that has not been intentionally altered, filtered or manipulated.

1. Electronic Surveillance (Wiretap)

Surreptitious electronic monitoring of conversations differs from consensual surveillance techniques in that no party to the surreptitiously monitored conversation need have consented to, or have knowledge of the fact that the recording is occurring. Surreptitious recordings are so intrusive into the privacy rights of individuals that Congress provided protection in federal law.[64] Additionally, state legislatures have followed suit and most state laws now generally mirror federal law. Thus, in order to place a wiretap onto a telephone, the government must obtain a court order, and the review process in most jurisdictions prior to seeking a wiretap is a stringent one. Still, district courts approve the vast majority of wiretap applications.[65]

Law enforcement agencies often seek wiretaps due to the belief that there is no better evidence of guilt than an individual's own words. The use of this technique to gather evidence has increased. In 2003 the total number of wiretaps approved by the courts, both federal and state, exceeded 1,400 and wiretap use increased by 6 percent over the previous year.[66] The states of New York, New Jersey, California, Florida, Maryland, Pennsylvania and Illinois combined accounted for 90 percent of all state wiretaps issued.[67] Federal agencies obtained 864 wiretaps in 2003.[68] These court orders

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[64] *See* 18 U.S.C. § 2510, *et. seq.*

[65] http://www.uscourts.gov/Press_Releases/03wtreport.pdf

[66] *Id.*

[67] *Id.*

[68] *Id.*

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included surreptitious recordings of telephone conversations, as well as digital phone pagers, voice pagers, facsimile machines and electronic mail.[69] While the bulk of these wiretaps still involve narcotics investigations, corporate investigators are increasingly utilizing this technique in white collar investigations.

Agents obtain warrants authorizing wiretaps through a complex approval process, which includes agency review and ultimately judicial approval and oversight.[70] Authorization for a wiretap generally requires a showing that normal investigative procedures have been tried and failed or reasonably appear too dangerous or unlikely to succeed.[71] Wiretaps are only valid for 30-day intervals, but may be extended for additional 30 day periods upon request.[72] They are to be implemented so as to minimize interception of communications that fall outside court order or that contain attorney-client privileged information.

2. Consensual Audio or Video Surveillance

"Consensual" audio taping of communications is not a search within the meaning of the Fourth Amendment.[73] Under federal law, only one party to the conversation must give permission to records its contents in order for the recording to be consensual.[74] Thus, an employee may secretly record conversations with other employees or senior management. However, many states require all parties to a conversation to give permission before the conversation legally can be recorded. However, when law enforcement agents are acting within their investigative duties, only one party's consent is necessary in order for the conversation to be recorded. Thus, law enforcement investigators are permitted to tape record conversations if one individual to the conversation–such as an undercover officer of a cooperating witness–consents to the recording,–regardless of the lack of probable cause or a court order.[75]

The use of an undercover video recording, however may be done without the consent of any of the participants, if the recording is of activities that are held open to the public where there is no reasonable expectation of privacy. Thus, investigative agents may place video recorders to monitor business fronts, loading docks and the like without seeking court authority.[76]

3. Undercover Agents and Cooperating Witnesses

Both state and federal investigators commonly use undercover agents or cooperating witnesses to conduct investigations. Undercover agents can be used to conduct "sting" operations or just to gather information. Again, while in the past undercover agents have been more commonly identified with street crimes, their use has become more standard in the investigation of commercial

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69 *Id.*

70 18 U.S.C. § 2510 *et. seq.*

71 18 U.S.C. § 2518(1) (a)-(f).

72 18 U.S.C. § 2518(5).

73 U.S. Attorney Manual § 9-1.301; *United States v. White*, 401 U.S. 745 (1971).

74 *See United States v. Davis*, 780 F. 2d 838, 846 (10th Cir. 1985); 18 U.S.C., § 2511(2)(d).

75 U.S. Attorney Manual § 9-1.301; *United States v. White*, 401 U.S. 745 (1971); s*ee also* 18 U.S.C., § 2511 (2)(c) ("[I]t shall not be unlawful…for a person acting under color of law to intercept a wire, oral, or electronic communication, where such person is a party to the communication or one of the parties to the communication has given prior consent to such interception.")

76 *See generally*, U.S. Attorney Manual §9-7.210.

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industries. The Supreme Court has recognized that using undercover agents is not a per se violation of the Fourth Amendment.[77] Undercover agents, who secretly meet with business executives and tape record those meetings, have been utilized in several high profile investigations of corporations. Perhaps the best known of these investigations was the prosecution of Archer, Daniels, Midland (ADM) and its executives for price fixing of lysine. The FBI recruited an employee of the corporation who agreed to secretly record conversations and meetings with company executives and others. As a result of the investigation and prosecution, ADM pled guilty and agreed to pay approximately $100 million in penalties.[78]

4. Trash Searches

A favorite law enforcement technique in narcotics investigations has become all too familiar with respect to corporate investigations. This tactic is effective in investigations of corporations because many such organizations do not have a comprehensive document destruction policy in place. If such a policy is in place, they too commonly are not sufficiently enforced. Accordingly, corporate documents containing sensitive or privileged material often find their way into the trash. Because refuse, set out for the express purpose of conveying it to a third party– the trash collector–loses any privacy protections, a search of that trash does not qualify as a search under the Fourth Amendment.[79] Accordingly, if the garbage is placed in a location accessible to the general public or where trash collectors regularly collect debris, the owner of the trash retains no privacy expectation in the contents of the trash and, thus, no warrant is required.

While the practical aspects of searching the trash of a large corporation may appear daunting, resourceful law enforcement agents have been known either to pay the trash collector to segregate the corporation's trash, or ride along with the trash collector to obtain the sought-after trash. Searching the trash of the homes of executives also is a common technique, especially after the service of a subpoena. This is done to determine if requested materials are being destroyed in lieu of production.

B. Overt

Overt investigative methods usually arise during the second stage of an investigation. Such techniques generally are employed after a corporations has been made aware of an investigation. Overt investigative methods may be the first indication to a corporation that it is under investigation. These investigation methods include both voluntary requests for information and court orders to provide information.

1. Search Warrants

Executing search warrants against corporate entities at their offices and facilities is a common occurrence in the government's investigation of corporate misconduct. These warrants often are accompanied by coordinated efforts by law enforcement agents to locate and interview corporate officers or employees without notice. This tactic has tremendous ramifications on corporations and

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77 *Lewis v. United States*, 385 U.S. 206 (1966).

78 http://www.usdoj.gov/opa/pr/1996/Oct96/508at.htm

79 *California v. Greenwood*, 486 U.S. 35 (1988); *United States v. Chapman*, 196 F. Supp. 2d. 1279, 1282 (M.D. Ga. 2002).

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other types of business organizations. Not only does the execution of a search warrant have a potentially devastating impact on the corporate officers, employees and customers, it also interferes with the corporation's ability to continue to conduct day-to-day operations and defend itself against criminal charges. The inadvertent release of privileged material seized in a search warrant also poses serious problems for corporate entities, which are heightened by the potential that damaging information will be provided by employees during simultaneous coordinated interviews conducted by agents at multiple locations.

The Fourth Amendment provides two separate protections related to these investigative techniques.. First, the Fourth Amendment protects the "right of the people to be secure in their persons, house, papers and effects against unreasonable searches and seizures." Second, as discussed above, it also provides that "no warrants shall issue, but upon probable cause, supported by oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized."[80] However, these protections only apply to activities conducted by government agents. They do not apply to the actions of private citizens.[81] Thus, documents or other information taken by rogue employees or whistle blowers–without direction or prodding of law enforcement officers–and later turned over to authorities may be used by the law enforcement against others, including the corporation, absent some improper influence by law enforcement on the employee.[82]

The Fourth Amendment protections provided to an individual's house extend to many commercial and business premises as well.[83] As a practical matter, the Supreme Court requires that the government obtain a warrant, based upon probable cause, prior to initiating a search, unless the search falls within a recognized exception.[84] Probable cause exists when there are reasonable grounds to believe that evidence or fruits of crimes are presently located in the particular place to be searched.[85] If a search has been conducted in violation of the Fourth Amendment, the evidence obtained generally will not be permitted into evidence in the government's case-in-chief, absent an officer's demonstration of good faith.[86]

a. General Concepts

To obtain a search warrant, agents or other law enforcement officers must seek warrant from a judge located in the district where the property to be searched is located.[87] The warrant consists of an application, the warrant itself and a sworn affidavit by a law enforcement officer or attorney. These documents must establish that there is probable cause to believe that at the place to be searched the agents will find: (1) evidence of a crime; (2) contraband, fruits of a crime, or other items illegally possessed; (3) property designed for use, intended for use, or used in committing a crime; or (4) a person to be arrested or a person who is unlawfully restrained.[88] Often, the underlying affidavit which establishes the probable cause will be sealed by the court and unavailable for review during

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80 U.S. Const., Am 4.

81 *Burdeau v. McDowell*, 256 U.S. 465 (1921).

82 *United States v. Feffer,* 831 F.2d 734, 738 (7th Cir. 1987).

83 *New York v. Burger*, 482 U.S. 691 (1987).

84 *Minnesota v. Dickerson*, 508 U.S. 366, 372 (1993).

85 *Steagald v. United States*, 451 U.S. 204 (1981).

86 *Weeks v. United States,* 232 U.S. 383 (1914) (exclusionary rule); *Leon v. United States*, 468 U.S. 897 (1984) (good faith exception to exclusionary rule).

87 Fed. R. Crim. P. 41 (b).

88 Fed. R. Crim. P. 41 (d)(1).

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the search or immediately thereafter. While Federal Rule of Criminal Procedure 41 does not address the authority of courts to seal the accompanying affidavit, courts have the inherent authority to control their own papers filed with the courts, within certain constitutional limits.[89] However, most search warrants are sealed upon the motion of the prosecutor, who may wish to prevent dissemination of details of an ongoing investigation.

The place to be searched must be described with particularity. The Fourth Amendment's safeguard of particularity is designed to mandate "a description which particularly points to a definitely ascertainable place so as to exclude all others."[90] This requirement insures that the officers conducting the search will not search the wrong location, for which no legal authority exists. The search warrant must also set forth, with particularity, the items that the judge has authorized the agents to seek. The search warrant gives law enforcement officers the right to search anywhere on the premises described in the search warrant where the items might be located. Although this right includes utilizing force to enter an area to search, agents must knock and announce their presence before doing so unless certain exigent circumstances exist. .

b. General Precautions

Search warrants are executed with no advance warning. Accordingly, it is important that a corporation have specific business practices in place that will facilitate responding to a search warrant and insure that the corporation's interests are protected. These practices include:

- Clearly mark and segregate all attorney-client privileged documents;
- Maintain computer back-up tapes off-site. This allows for general security of corporate information technology, as well as insuring access to day-to-day operations should the agents seize all computer equipment.
- Maintain emergency contact numbers in a readily available location. This list should include the general counsel, key corporate personal and a criminal defense attorney who is experienced with representing corporations in such situations.
- Create an inventory of all computer hardware and software to re-establish day-to-day operations, should agents seize all computer equipment.
- Maintain a duplicate of payroll, accounts receivable and accounts payable records at an off-site location. This allows for general security of necessary corporate information, as well as the facilitating of day-to-day operations should the agents seize all related documents.
- Key employees should be identified and receive advance training regarding what actions to take.
- Human Resources should develop a plan to send all non-essential employees home during the execution of the search warrant.

c. Execution of the Search Warrant

The actions taken by the corporate employees and officers while the search warrant is being executed are crucial for both the corporate employees and ultimately, the corporation itself. The

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89 *Matter of Sealed Affidavit(s) to Search Warrant Executed on February 14, 1979*, 600 F.2d 1256, 1257 (9th Cir. 1979), citing *Nixon v. Warner Communications Inc*., 435 U.S. 589 (1978).

90 *People v. Watson*, 186 N.E. 2d 326 (1962); *See also United States v. Gahagan*, 865 F.2d 1490 (6th Cir. 1989); *United States v. Gitcho*, 601 F.2d 369 (8th Cir. 1979).

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following is a checklist of steps that must be taken by the corporation during the execution of a search warrant:

- An employee should be instructed to immediately contact the individuals previously identified in the emergency contact list.
- A key employee should review the warrant immediately upon presentation by the agents to insure a full understanding of the scope and limitations imposed by the judge. This will include the locations to be searched and items for which the search was authorized. Keep in mind, however, that for all practical purposes, any objections a corporate employee might have to the warrant or its scope are meaningless: agents are not required to stop or limit a search simply because an occupant of the target premises contest the legality of the warrant or the search. Instead, instruct an employee to make a list of the alleged improprieties and material which he or she contests has been improperly seized, and present it to defense counsel so he or she can file a motion to suppress.
- The employees should be instructed not to become argumentative or interfere with the agents conducting the search and not to hide, destroy or change any documents or evidence.
- If the agents ask for consent to search any property or area, or to seize any property, that consent generally should not be given.
- The agents should be asked to speak with the general counsel or experienced outside counsel.
- Counsel should instruct the agents that the attorney desires to be present during the interview of any employee.
- Counsel for the corporation must identify any potential conflicts caused by the representation of employees during an interview.
- Generally, allowing the agents to interview corporate employees during the execution of the search warrant, outside the presence of counsel, is strongly discouraged.
- The agents should be instructed regarding how the attorney-client privileged documents are marked and their location and that there is **NO** waiver of that privilege. If agents attempt to seize privileged documents, counsel should object and make clear that the documents are privileged. If the agents insist on seizing the privileged material, counsel should immediately contact prosecutor and propose that the documents be sealed until the privilege can be litigated. A detailed listing of the privileged material should be made immediately.
- Insure that a copy of the inventory of seized property is obtained. At all times, if allowed, a key employee should accompany the searching agents and take notes of the locations searched, the items reviewed and a listing of the items seized.
- The identities of the searching agents should be obtained, if possible.
- All unnecessary employees should be excused from the premises for the remainder of the search. This will minimize the chance for interviews with the employees.
- All employees should be notified that the agents have the authority to search and seize under the search warrant but that there is no requirement for the employees to answer questions by the agents. This situation is crucial, as the agents will attempt to interview as many employees as possible. Improperly advising employees at this time may lead to charges of obstruction of justice. It is therefore imperative that any advice to the employees on this subject come from an experienced lawyer.

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- Counsel should immediately interview every person who spoke with agents regarding the nature of the questioning and the responses given, if any.
- Be prepared for the publicity surrounding the execution of the search warrant. It is possible that the media will have mobile cameras on scene. They do not have access to the premises and should not be allowed on site during the search. Employees should be strongly discouraged from speaking to the media.

d. Post Search Warrant

The time immediately following the execution of the search warrant is very important. The corporation's computer hardware and software likely will have been seized. It is important that the payroll, accounts payable and accounts receivable be returned to normal as soon as possible. This will necessitate that the corporation obtain replacement hardware and software, as well as duplicate records. Additionally, the psychological impact of the search on the employees and customers must be considered. The media will likely be very interested in the fact that a search warrant was executed at a business location and it will be important to have a well conceived, coordinated media plan in place. However, any statements should be made only after learning as much information as possible so as to minimize the potential for inaccurate statements that can lead to additional negative publicity or criminal liability.

The most important task at hand immediately after the execution of the search warrant is to learn the basis of the government's investigation. This information may lead to concerns regarding: whether rogue employees have placed the corporation at risk; whether corporate information should be segregated or access should be restricted; whether conflicts of interest have arisen; and whether the fiduciary responsibilities of officers and directors require action. For the duties and responsibilities of corporate management when confronted with allegations of misconduct, see Section IV of this InfoPAK. Additionally, senior management should immediately consider retaining the services of a media relations firm if the corporation does not have the ability to handle crisis management.

If property is seized as a result of a search warrant, a corporation has two potential methods of recovery. The first is to approach the prosecutor in charge of the investigation. If there are legitimate reasons for the return of, or access to, certain property such as accounts receivable, accounts payable, inventory or payroll, or particular software applications that are needed to run the day-to-day operations of the business, arrangements can often be made to allow continued operations. The second method of recovery is through the courts. Federal Rule of Criminal Procedure 41(g) allows a motion to be filed in the district where the property was seized for the return of the property. This rule allows for the court to return the property and if appropriate to impose reasonable conditions to protect access to the property and its later use in any proceedings.

If a search warrant is executed, a criminal investigation is being conducted and these matters should be discussed with an experienced White collar defense attorney immediately.

e. Search and Seizure of Computers

The escalating use of computers to assist in business operations, as well as the desire of government agencies to seek electronic evidence as a means of conducting a thorough investigation, has led to specific concerns regarding the search and seizure of computer evidence. There are a number of statutes and constitutional considerations that must be adhered to in any search and seizure of computer information, including the Fourth Amendment, the Privacy Protection Act, the Electronic

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Communications Privacy Act, and the USA PATRIOT Act. The rules regarding searching computers are extremely fact-dependant and vary based upon whether there is a search warrant or warrantless search, whether the place to be searched is a public or private employer, and whether there are others who have access. Due to the complexity of the issues, and the fact-dependant nature of any inquiry into this area, only a broad overview of searches conducted with a warrant as a result of a government investigation is discussed herein.[91]

i. Constitutional Considerations

"The legal framework for searching and seizing computers with a warrant largely mirrors the legal framework for other searches and seizures."[92] Generally, government agencies may obtain a search warrant to search and seize computer equipment and electronic data if they can meet the requirements of Federal Rule of Criminal Procedure 41, as discussed above. However, computers and electronic evidence present several additional concerns for agencies, as well as businesses. The technology involved in computers and electronic evidence often requires that agents execute the warrant in a fashion that differs significantly from the traditional search warrant. First, is the computer hardware itself contraband, evidence or an instrumentality of the crime, or is it merely being utilized as a storage device? If the computer both stores and transmits relevant evidence then the hardware is itself an instrumentality of the crime.[93] If however, the computer merely stores evidence, then Rule 41 arguable does not authorize seizing the hardware.[94]

ii. Statutory Considerations

The Privacy Protection Act,[95] passed by Congress in 1980, makes it unlawful for government agents to search or seize certain defined materials. These materials are generally associated with First Amendment activities. The viability of this Act is dubious today, however, as it was passed when the use of computers and the Internet were not as prevalent as they are now. Additionally, the language of the law is broad and includes materials by people or businesses that may now qualify for its protections due to the ease of publication.[96] While violation of this statute does not give rise to grounds for suppression, it can lead to civil damages against the government agents.[97] Additionally, there is currently a split of authority regarding whether even incidental violations of the Privacy Protection Act will result in civil damages against the agents.[98]

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91 For an exhaustive review of the relevant law regarding search and seizure of computers under all circumstances, see *Searching and Seizing Computers and Obtaining Electronic Evidence in Criminal Investigations*, 2nd Edition, Computer Crime and Intellectual Property Section, Criminal Division, United States Department of Justice (2002) http://www.cybercrime.gov/s&smanual2002.htm#introduction

92 *Searching and Seizing Computers and Obtaining Electronic Evidence in Criminal Investigations*, 2nd Edition, Computer Crime and Intellectual Property Section, Criminal Division, United States Department of Justice (2002) at 55, http://www.cybercrime.gov/s&smanual2002.htm#introduction

93 *See, Davis v. Gracey*, 111 F.3d 1472, 1480 (10th Cir. 1997).

94 *See, United States v. Tamura*, 694 F.2d 591, 595 (9th Cir. 1982).

95 42 U.S.C. § 2000aa.

96 See, *Searching and Seizing Computers and Obtaining Electronic Evidence in Criminal Investigations*, 2nd Edition, Computer Crime and Intellectual Property Section, Criminal Division, United States Department of Justice (2002) at 67-75, http://www.cybercrime.gov/s&smanual2002.htm#introduction

97 42 U.S.C. § 2000aa-6(d), 2000aa-6(a), (e).

98 *Steve Jackson Games, Inc. v. Secret Service*, 816 F. Supp. 432 (W.D. Tex. 1993), *aff'd on other grounds*, 36 F.3d 457 (5th Cir. 1994); *But see also*, *Guest v. Leis*, 255 F.3d 325 (6th Cir. 2001).

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Government investigations often include searches performed at Internet service providers to obtain information about the computer usage of individuals or businesses. The Electronic Communications Privacy Act,[99] passed by Congress in 1986, provides network account holders statutory privacy rights protecting stored account information that is held by network service providers. This statute is complex and was amended by the USA PATRIOT Act to specifically allow this type of information to be obtained via a search warrant issued by a court with jurisdiction over the offense under investigation, as opposed to a court within the territory where the property is located.[100] Of note, however, the USA PATRIOT Act has a specific sunset provision applicable to this amendment that, absent Congressional action, expires on December 31, 2005. Like the Privacy Protection Act, this law will not, absent constitutional violation, result in suppression of the evidence.[101] Instead, civil damages are the only remedy.[102]

iii. Practical Considerations

Searching and seizing computers generally requires specifically trained agents who are skilled at collecting electronic evidence without destroying or altering its contents. Electronically stored evidence is highly susceptible to destruction through negligence, inattention to detail or electronic "booby traps." These agents often ask company personnel to assist them in locating information within the computer files, to include specific documents, spread sheets or other compiled data.

Corporations should carefully determine whether to assist agents. While this assistance may speed their progress, the agents will be asking questions and obtaining answers that may later be relevant to their investigation and against the interests of the corporation and its management team or employees. At this stage of the investigation, it is highly unlikely that the corporation will know the nature and scope of the investigation, and thus the corporation will be unable to determine whether information given to agents will be against its interests.

Due to the geographical restrictions placed upon search warrants by the Fourth Amendment and by Rule 41, a search warrant that seeks and obtains electronic data stored or located within a computer network at a location outside the territory in which the corporation is located or perhaps even outside the United States, may result in suppression of the evidence. While several courts have addressed this issue and have not suppressed this evidence, the state of the law in this area is not settled.[103] Additionally, if an employee assists the agent in locating and obtaining the information sought by the agents, the government will also be in a position to argue that a corporate representative consented to bringing in the material to the territory.

Many electronic files contain privileged material. Thus, to properly protect this privilege, counsel should immediately notify the searching agency and the supervising attorney that privileged information is within the seized electronic evidence and that the corporation is asserting its privilege. Additionally, if possible, corporate counsel should obtain a copy of the seized material and review it so that protections can be specifically sought for the privileged material. This avenue is completely dependent upon the willingness of the prosecutor to provide such an accounting,

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[99] 18 U.S.C. §§ 2701-2712.

[100] See USAPATRIOT Act § 220, 224, 115 Stat. 272, 291-92, 295 (2001).

[101] 18 U.S.C. § 2708.

[102] *Id.*

[103] *United States v. Ramirez*, 112 F.3d 849 (7th Cir. 1997); *United States v. Martinez-Zayas*, 857 F.2d 122 (3rd Cir. 1988).

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however. Often the investigating agencies will create a "taint team" to review any privileged material. After this review, non-privileged material is provided to the investigating agents and the privileged material withheld. However, consideration should be given to requesting, or if necessary seeking court intervention, that the agencies do not review privileged material but instead seal it awaiting a court's *in camera* review, or the court's appointment of a special master to review it.

A detailed review should be made of the actual items seized to determine if they fit within the list of court-authorized items to be seized within the warrant.

Often the seizure of computers and electronic evidence leads to the introduction at trial of electronic mail (e-mail) contained within the computer systems. While the government has the burden to prove that a particular person received an email, the collective knowledge doctrine, previously discussed in Section II. A. 2, can be used against a corporation. Several courts do not require that the government prove at trial that particular e-mails were opened or read. With increasing frequency, however, proponents of email evidence are required to prove that addressees received, opened, and read electronic correspondence, memoranda and attachments to email communications.[104]

Due to the technical requirements in obtaining the information, backlog of cases, and the sheer quantities of materials, the process of examining seized computers is extremely lengthy, often taking several months. Neither the Fourth Amendment nor Rule 41 require that the examination must take place within any particular time. However, several courts have imposed a time limit under the theory that an exceedingly lengthy process is "unreasonable."[105]

2. Subpoenas

a. Grand Jury

The authority of the grand jury to issue subpoenas arises from its function (1) to determine whether probable cause exists to return an indictment, and (2) to investigate potential criminal activity.[106] Any activity involving a grand jury, whether state or federal, usually signifies that a criminal investigation is being conducted. There are two distinct types of grand jury subpoenas. *Subpoenas ad testificandum* require witnesses to appear before the grand jury and provide sworn testimony, absent a privilege. *Subpoenas duces tecum* require the production of physical evidence, such as documents, records and the like. In *Branzburg v. Hayes*, [107] the Supreme Court stated that the grand jury "has the right to every man's evidence." The grand jury's power, though very broad, does have certain limitations imposed either by the Constitution or by various privileges.

In *Hale v. Henkel*, [108] the Supreme Court applied the dictates of the Fourth Amendment to subpoenas. The Fourth Amendment requires that the subpoena be relevant to the inquiry of the grand jury, reasonable in its scope and particular in its demands.[109] Although the Fourth

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[104] *See, e.g., Campbell v. Gen'l. Dynamics Gov't. Systems Corp.*, 321 F. Supp. 2d 142, 145 (D. Mass. 2004).

[105] See *Searching and Seizing Computers and Obtaining Electronic Evidence in Criminal Investigations*, 2nd Edition, Computer Crime and Intellectual Property Section, Criminal Division, United States Department of Justice (2002) at 111-115, http://www.cybercrime.gov/s&smanual2002.htm#introduction

[106] *United States v. R. Enterprises*, 498 U.S. 292, 296 (1991).

[107] *Branzburg v. Hayes*, 408 U.S. 665, 688 (1972).

[108] *Hale v. Henkel*, 201 U.S. 43 (1916).

[109] *United States v. R. Enterprises*, 498 U.S. 292 (1991).

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Amendment very infrequently will constitute as a basis upon which to quash a subpoena, such motions are rarely granted. A subpoena must describe the requested material with sufficient clarity to permit compliance, and yet not be so broad as to be oppressive.[110] In *In re Grand Jury Proceedings (General Motors Corp.),*[111] a subpoena for corporate documents, covering essentially every aspect of a corporation's internal and external activities, was quashed on the grounds that it was overbroad. While the Fifth Amendment provides a basis for a "person" to refuse to provide evidence against himself, corporations have no such right.[112] Accordingly, corporations must provide incriminating material, absent a legitimate basis for challenging the authority of the subpoena or the application of a specific privilege.

The Federal Rules of Criminal Procedure set forth the requirements of subpoenas, including grand jury subpoenas. A subpoena must describe the requested material with sufficient clarity to permit compliance, and yet not be so broad as to be oppressive. A grand jury subpoena may be quashed or modified by a court if it is found that "compliance would be unreasonable or oppressive."[113] Although a party commanded to appear before the grand jury should not expect reimbursement for the expense of testifying,[114] courts have occasionally required the government to pay the cost of compliance.[115]

i. Subpoenas Duces Tecum

Pursuant to Federal Rule of Criminal Procedure 17, a grand jury may subpoena "any books, papers, documents, data or other objects the subpoena designates." The subpoena, therefore, may require an individual or corporation to produce its payroll records, bank statements, accounting documents, contracts, email, policy and procedure manuals, computers, hardware, software, minutes of the board of directors' meetings, compensation figures, internal decision making documents, and correspondence files.

In most cases, copies may be provided to the grand jury; however, there are instances where originals must be produced. The power of the grand jury is such that originals are within its right to demand.[116] Additionally, as a result of the influx of computers in the corporate setting, subpoenas routinely require the production of all electronic records. This requirement for production can be extremely burdensome and tremendously expensive, as vast quantities of documents must first be located in the electronic files, then copied, categorized, reviewed for relevancy and privileges, and then provided to the grand jury or its agent.

ii. Subpoenas ad Testificandum

Individuals who are subpoenaed to provide testimony before a grand jury may be classified as: (1) fact witnesses; (2) subjects; or (3) targets. "Fact witnesses" are individuals who have some factual knowledge about the allegations under investigation, but are not viewed by the grand jury or the

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110 *See In re Grand Jury Subpoena Duces Tecum to John Doe Corp.*, 570 F. Supp. 1476, 1478-79 (S.D.N.Y. 1983).

111 *In re Grand Jury Investigation,* 174 F. Supp. 393 (S.D.N.Y. 1959).

112 *Bellis v. United States*, 417 U.S. 85 (1974).

113 Fed. R. Crim. P. 17 (c)(2).

114 *In re Grand Jury No. 76-3*, 555 F. 2d 1306, 1309; See, e. g., *Hurtado v. United States*, 410 U.S. 578, 589 ("public obligation . . . persists no matter how financially burdensome").

115 *In re Morgan*, 377 F. Supp. 281, 284-85 (S.D.N.Y. 1974); *In re Grand Jury No. 76-3*, 555 F.2d 1308-09.

116 See *In re August, 1993 Regular Grand Jury*, 854 F. Supp. 1392, 1402 (S.D. Ind. 1993).

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prosecutor as having any criminal liability. "Subjects" are individuals "whose conduct is within the scope of the grand jury's investigation."[117] A "target" is someone "to whom the prosecutor or the grand jury has substantial evidence linking him or her to the commission of a crime and who, in the judgment of the prosecutor, is a putative defendant."[118] While the prosecutor may call corporate employees into the grand jury and advise them of their individual status, the corporate status may not be readily apparent, or even disclosed.

It is the policy of the Department of Justice to provide any individuals who are "subjects" or "targets" subpoenaed to appear before a grand jury an "Advice of Rights."[119] An Advice of Rights informs the witness that:

- The grand jury is conducting an investigation of possible violations of Federal criminal laws involving a particular subject matter.
- The person may refuse to answer any question if a truthful answer to the question would tend to incriminate him.
- Anything the person does or says may be used against him by the grand jury or in a subsequent legal proceeding, and
- If the person has retained counsel, the grand jury will permit him a reasonable opportunity to step outside of the grand jury room to consult with counsel if he desires.

If the subpoenaed individual is a "target", as opposed to "subject", he should also be advised that "the witness's conduct is being investigated for possible violation of federal criminal law." Further, in addition to providing a written copy of these rights, the prosecutor will also verbally advise the individual of these rights on the record and have the witness affirm that he understands them.[120]

During his or her testimony before a grand jury, a subpoenaed witness may be questioned by either the prosecutor or the grand jurors. Although the prosecutor initiates the questioning, it is common practice for government counsel to solicit questions from the grand jury at the end of his or her examination of the witness. As there are no rules of evidence, a witness will be permitted to testify as to both hearsay and personal knowledge.[121] Additionally, because a witness has no right to have either individual or corporate counsel in the grand jury room during his or her testimony, great care should be taken in preparing the witness prior to testifying, and a thorough debriefing should be conducted after the testimony. Statements given in a grand jury setting by corporate employees can have a significant impact on the corporation. Additionally, because grand jury witnesses are permitted to discuss what took place in the grand jury room while government agents are precluded from doing so,[122] the corporation is at a severe disadvantage if its employees are subpoenaed and the corporation has not taken the proper measures to learn the scope of the information provided to the government.

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117 U.S. Attorney Manual, §9-11.151.
118 *Id.*
119 *Id.*
120 *Id.*
121 U.S. Attorney's Manual § 9-11.232.
122 Fed. R. Crim. P. 6 (e).

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iii. Practical Considerations

It is essential that corporations prepare their employees prior to testifying before the grand jury. Lack of proper preparation can expose the corporation to significant risk, since the statements of the employee may be used later against the corporation.. If a witness is properly prepared, however, it may be possible to persuade a grand jury not to indict or, at least make the grand jury aware of certain facts that may mitigate charges that ultimately are brought against the corporation. Further, because the prosecutor is not required to present exculpatory evidence to the grand jury,[123] it is especially important that witnesses for the corporation be thoroughly prepared, as they are likely to be a corporation's only opportunity to present favorable evidence to the grand jurors. In all practicality, however, a corporation should not expect to win at this level. The old adage that "a grand jury will indict a ham sandwich" is a popular notion that is reaffirmed by the frequency with which indictments are returned.

When a corporation first learns that an employee has been subpoenaed to appear before the grand jury, there should be an immediate discussion with an experienced criminal defense counsel familiar with the intricacies of corporate investigations. While it may be that the investigation at the time of the employee's testimony does not center on the corporation, grand juries have often delved into areas far afield from those first under consideration. The employee should be immediately interviewed about his knowledge of the events that lead to the subpoena and any potential conflicts that may exist with the corporation. In addition, subpoened employees should be advised about testifying and maintaining corporate privileges, and a determination should be made regarding whether independent counsel should be retained on their behalf.[124] Additionally, corporate management should review the by-laws and state statutes regarding the employee's right of indemnification for the costs associated with any representation.[125]

To successfully prepare a witness to testify before the grand jury, counsel will want to consider instructing the witness on the following points:

- First and foremost: tell the truth;
- Discuss his testimony outside the grand jury room only with counsel;
- Do not create documents solely for production via the subpoena, and do not destroy or alter documents;
- Carefully review any document or exhibit shown to him in the grand jury before answering questions about it;
- He has the right to have counsel, although counsel will not be permitted to accompany him inside the grand jury room during his testimony;
- He can consult with counsel if he is confused or needs legal advice during his testimony;
- Do not be reluctant to say he does not know the answer, if that is a truthful answer;
- Do not guess, speculate or assume;
- Answer only the question that is asked;
- Do not volunteer additional information;

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123 *See United States v. Williams*, 112 S.Ct. 1735 (1992).

124 See also, Section VI. D. of this InfoPAK on Joint Defense Agreements.

125 See Section V. B. 1.of this InfoPAK for further discussion on this topic.

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- Avoid arguing with the prosecutor or grand juror during questioning (You will always lose such a battle);
- Avoid answering compound questions;
- Avoid long narrative answers;
- Distinguish personal knowledge from information heard from others;
- Be wary of questions that assume facts not known;
- Remain calm;
- Be prepared to recall, with as much specificity as possible, the subjects covered during the testimony.[126]

b. Administrative or Regulatory

i. Inspector General

In 1978, Congress passed the Inspector General Act,[127] which established the position of Inspector Generals in many federal agencies. The inspector generals were given the power to issue administrative *subpoenas duces tecum* to obtain documents to "conduct and supervise audits and investigations relating to the programs and operations of the designated federal agencies."[128] The evidence obtained through these administrative subpoenas may be used for administrative proceedings, or for civil or even criminal actions. However, the subpoena must be issued within the proper scope of the statutory authority of the inspector general.[129] However, this authority does not extend to the ability to require testimony.

ii. Authorized Investigative Demands

In 1996, Congress passed the Health Insurance Portability and Accountability Act[130], which among many other changes, gave federal prosecutors the ability to issue Authorized Investigative Demands in health care related investigations.[131] These administrative subpoenas provide more flexibility for federal prosecutors to share the results of criminal investigations with civil attorneys, which otherwise can be limited by grand jury secrecy rules.[132] These subpoenas require the production of documents, as well as testimony by the custodian of the records concerning the production and authenticity of the records.[133] A territory restriction is built into the limitations of the subpoena, such that a production will not be required more than 500 miles from the location of the business that was served with the subpoena.[134] This territorial limitation however, is often negated by cooperation between offices of the Department of Justice, or by the corporation's decision not to enforce the limitation.

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126 See, Dan K. Webb, Robert W. Tarum, & Steven F. Molo, *Corporate Internal Investigation,* Law Journal Press, § 12.04[1] and [2], 2003.
127 Pub. L. 95-452, 92 Stat. 1101, 5 U.S.C. App. 3.
128 5 U.S.C. App. 3, § 2(1).
129 *See, e.g., United States v. Montgomery County Crisis Center*, 676 F. Supp. 98 (D. Md. 1987).
130 Pub. L. 104-191, 110 Stat. 1936.
131 18 U.S.C. § 3486.
132 Fed. R. Crim. P. 6(e).
133 18 U.S.C. § 3486 (a)(1)(B)(i), (ii).
134 18 U.S.C. § 3486 (a)(3).

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The law also allows the government to request an *ex parte* court order prohibiting the recipient from disclosing the existence of the subpoena for a period of 90 days in order to keep the investigation confidential.[135] Additionally, absent a court order, any health information about an individual that is obtained as a result of this subpoena may not be used in any administrative, civil or criminal proceeding or investigation unless it arises out of and is directly related to receipt of health care, payment for health care or a fraudulent claim related to health care.[136]

The receipt of an Authorized Investigative Demand should immediately be seen as a "red flag" for a corporation, as the use of this investigative technique, like that of a grand jury subpoena, indicates that a criminal investigation is underway.

iii. Securities and Exchange Commission

In conducting investigations into potential securities laws violations, the Securities and Exchange Commission has the authority to issue subpoenas both for documents and testimony. The Commission is "authorized to investigate any facts, conditions, practices, or matters which it may deem necessary or proper to aid in the enforcement of such provisions in the prescribing of rules and regulations" under the securities laws.[137] The Securities and Exchange Commission has the ability to conduct both informal and formal investigations. When conducting informal investigations, the SEC does not have the authority to issue subpoenas. However, if SEC lawyers seek and obtain approval from the Commissioners to open a formal investigation, they can acquire that authority.[138]

3. Interviews

Once a government agency has initiated an investigation, the investigator or prosecuting attorney may contact employees at the target corporation directly and request that the individuals meet with investigators to discuss the issues under investigation. To the extent possible, employee interviews need to be handled appropriately and in the presence of counsel. Agents conduct employee interviews not only to gather information, but also to "lock" individuals into a position on issues relevant to their investigation. In this respect, admissions or unfavorable statements made by an employee can be used against a corporation in a civil or criminal proceeding.

Often, employees are contacted in an informal manner at their home or business and asked to consent to an interview. An individual may speak to the agent at that time, but is under no obligation to do so. Instead, the individual may inform the agent that he wishes to speak to counsel before any interviews occur. If the individual already has personal counsel at the time he is contacted, he may want to call his attorney when the agents arrive so counsel can speak to the agent directly, determine who the agents work for, and identify the subject matter of the investigation. If the individual contacts corporate counsel instead of his private attorney, corporate counsel should ascertain whether the interview relates to company matters and, if so, whether the employee wants corporate counsel at the interview.[139] Corporate counsel cannot direct the employee to decline the interview, but should strongly encourage the employee to retain his own attorney or permit corporate counsel to attend to protect the employee's and the corporation's interests.

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[135] 18 U.S.C. § 3486 (a)(6)(A).
[136] 18 U.S.C. § 3486 (e)(1).
[137] 15 U.S.C. § 78u(a)(1).
[138] 15 U.S.C. § 78u(b).
[139] Webb, § 13.02[1].

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If in-house counsel learns that a corporate employee has been interviewed without an attorney, he or she should immediately debrief the employee regarding the content of the interview. Often the questions an agent asks provide helpful insight into the subject matter of the investigation, the individuals the agent believes are involved and the how long the investigation has been under way. In this respect, the employee should be asked to provide as much specific detail as possible about the interview, including the subjects covered, the names of individuals the agent was interested in and any documents the employee was shown.[140]

4. Foreign Evidence Collection Methods

With the advent of international trade and multi-national corporations, as well as foreign-based, wholly owned subsidiaries, the need for investigative agencies to extend their reach across borders has become increasingly apparent. Additionally, with corporate investigations into such offenses as the Foreign Corrupt Practices Act[141] and the International Emergency Economic Powers Act,[142] as well as the increase of tracings of business relationships and financial transactions, the techniques used by governmental agencies to gather this evidence are becoming more prevalent.

a. Letters Rogatory

Letters Rogatory are methods of securing court assistance in both the requesting jurisdiction, as well as the receiving jurisdiction to obtain evidence as a result of a government investigation.[143] Because of the nature of seeking court assistance in both jurisdictions, these requests are very time consuming.

b. Mutual Legal Assistance Treaties

Mutual Legal Assistance Treaties are agreements entered into by the United States and various other countries, for the purpose of assisting one another in law enforcement investigations and related matters. These agreements often will include the authority to subpoena documents, summon witnesses and seize assets.[144]

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[140] Webb, § 13.02[3].
[141] 15 U.S.C. § 78dd-1, *et. seq.*
[142] 50 U.S.C. § 1701, *et. seq.*
[143] 28 U.S.C. § 1781.
[144] Webb, § 13.08.

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IV. The Duties and Responsibilities of Corporate Management

Often, the first time that a corporation will learn of potential misconduct by its employees or agents is when confronted with a government investigation. This knowledge imposes a responsibility on officers and directors to insure that they act appropriately under the circumstances.

A. Allegations of Misconduct

Senior corporate officers who discover alleged misconduct as a result of a government investigation must determine whether an internal investigation should be undertaken. There are a number of factors to be considered in this analysis, including:

- The nature of the allegation;
- The nature of the government investigation;
- The credibility of the allegation or inquiry;
- The potential consequences if the allegation which led to the investigation is accurate;
- The potential consequences of the government investigation and any related collateral consequences;
- The length of time, complexity and cost of conducting an internal investigation;
- The potential costs associated with not conducting an internal investigation; and
- The public relations risks associated with this decision.

Deciding whether to conduct an internal investigation depends upon the nature and seriousness of the government's investigation and the underlying allegations, as well as the collateral issues that naturally flow from the fact of the allegation; the more serious the allegation and the consequences, the more likely an investigation will be required. Only by conducting an internal investigation will the corporation be able to: (1) determine the facts; (2) put a halt to ongoing misconduct; (3) remedy any problems that occurred; (4) prepare a comprehensive defense to possible regulatory, criminal or civil litigation, (4) establish relevant preventative measures; and (5) if ultimately charged with a crime or other misconduct, reduce the potential punishment or loss to the corporation or its senior management. (*See* ACC InfoPAK regarding Internal Investigations for a more detailed discussion).

B. Duties of Care, Obedience and Loyalty

Directors and officers owe fiduciary duties to the corporation, including the duties of care, obedience and loyalty.[145] These duties are imposed both through statutes and case law. The Model Business Corporation Act defines directors' and officers' duties of care. Under this Model Act, a director is required to "act (1) in good faith, and (2) in a manner the director reasonably

[145] *See, e.g., McCall v. Scott,* 250 F.3d 997 (6th Cir. 2001); *Gearhart Industries v. Smith International*, 741 F.2d 707 (5th Cir. 1984).

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believes to be in the best interests of the corporation."[146] Pursuant to the Model Act, officers are required to act "(1) in good faith; (2) with the care that a person in a like position would reasonably exercise under similar circumstances; and (3) in a manner the officer reasonably believes to be in the best interests of the corporation."[147]

The duty of obedience requires a director to act within the corporation's scope of powers, as set forth by its charter or by the laws of the state of incorporation, and mandates that directors not exceed those powers.[148] The duty of loyalty requires that a director act in good faith and that the director not allow personal interests to prevail over the interests of the corporation.[149] The duty of care requires that a director be diligent and prudent in managing the corporation's affairs.[150]

Corporate directors and officers have a duty of care to respond to allegations of corporate wrongdoing by fully investigating the accusations and by considering all pertinent information bearing on the issue. Thus, once a director or officer is put on notice of a claim of serious wrongdoing, he or she must put forth a reasonable effort to discover all relevant information to fulfill his or her duty of care.[151]

C. Personal Liability of Directors and Officers

1. Civil Liability

Directors and officers can be held civilly liable for their mere failure to investigate criminal misconduct.[152] Court decisions have stated that this theory of personal liability for breach of the duty to exercise appropriate attention concerning potential illegal corporate activities was "possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment."[153] Personal liability can occur from either an ill-advised board decision that resulted in a loss or an unconsidered failure of the board to act in circumstances in which due attention might have prevented the loss.[154]

Personal liability resulting from inaction or neglect is highly fact dependant. A director faces potential liability if the director "has recklessly reposed confidence in an obviously untrustworthy employee, has refused or neglected cavalierly to perform his duty as a director, or has ignored either willfully or through inattention obvious danger signs of employee wrongdoing."[155] Similarly, the Internal Revenue Code attaches civil liability to any "person required to collect, truthfully account for, and pay over any tax."[156] The Internal Revenue Code further defines "person" to include "any

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[146] Model Business Corporation Act 2000/01/02 Supplement, 3rd Edition, Section 8.30.
[147] Model Business Corporation Act 2000/01/02 Supplement, 3rd Edition, Section 8.42.
[148] *Gearhart Industries,* 741 F.2d at 719.
[149] *Id.* at 719.
[150] *Id.* at 720, citing Ubelaker, *Director Liability Under the Business Judgment Rule*, 35 Sw.L.J. 775, 784 (1981).
[151] See, e.g., *In re Abbott Labrotories Derivative Shareholders Litigation*, 325 F.3d 795 (7th Cir. 2003); *McCall v. Scott,* 250 F.3d 997 (6th Cir. 2001); *In re Caremark*, 698 A.2d 959 (Del. Ch. 1996).
[152] *See, e.g., In re Abbott*, 325 F.3d 795 (7th Cir. 2003).
[153] *McCall v. Scott,* 250 F.3d 997, 999 (6th Cir. 2001), quoting *In re Caremark*, 698 A.2d 959, 967 (Del. Ch. 1996).
[154] *Id.*
[155] *Graham v. Allis-Chalmers Mfg. Co.*, 188 A.2d 125, 130 (Del. 1963).
[156] 26 U.S.C. § 6672 (a).

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officer…under a duty to perform the act in respect of which the violation occurs."[157] Additionally, courts have held that under these sections of the law, corporate officers with authority to pay taxes are liable, regardless of whether they exercised their authority.[158]

Upon learning of misconduct, officers and directors must assess their fiduciary responsibilities of care, obedience and loyalty and carry out those duties. In general, state laws require directors to discharge their duties in good faith and in a manner they reasonably believe is in the corporation's best interests. In carrying out their duties, directors must employ the same care as an ordinarily prudent person in a like position would exercise under similar circumstances.[159] A director whose actions conform to this standard of conduct is immune from personal civil liability.[160] This principle is commonly referred to as the "Business Judgment Rule."

D. Business Judgment Rule

The Business Judgment Rule is a presumption that the directors of a corporation, when making a business decision, "acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."[161] This rule is premised on five fundamental elements: (1) the board of directors manages the affairs of the corporation; (2) the directors' management function consists of making economic decisions by weighing the potential benefits and risks and supervising the officers and employees of the business; (3) directors should be held accountable when their performance does not meet appropriate standards; (4) directors are not guarantors that the business will enjoy financial success; and (5) directors' culpability will occur when they breach their fiduciary duties.[162] This Rule articulates the manner in which directors exercise their duties, regardless or whether the directors' actions ultimately are determined in retrospect to be correct or wise. The Business Judgment Rule is process-specific, and ensures accountability while simultaneously "protect[ing] and promot[ing] the full and free exercise of the managerial power granted" to directors.[163] Consequently, directors generally are protected from mistakes of business judgment so long as their decisions do not involve fraud, illegality or conflicts of interest, and are consistent with the business purposes of the corporation.[164] The Delaware Court of Chancery states that even "stupid," "egregious" or "irrational" decisions will not support grounds for personal director liability if the decision making process was rational and if a good faith effort was made to advance corporate interests.[165]

Because the Business Judgment Rule only protects "informed" decisions, however, directors privy to allegations of misconduct must respond with due care by implementing appropriate procedures. One such procedure is an internal investigation.[166] An informed decision is defined as one in which

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157 26 U.S.C. § 6671 (b).

158 *United States v. Iverson*, 162 F.3d 1015, 1024 (9th Cir. 1998).

159 *See* 18B Am. Jur. 2d Corporations, § 1697 (2004).

160 *See* 29 Am. Jur. Proof of Facts 3rd, § 9.1-9.7 (2004).

161 *In re Abbott*, 325 F.3d 795, 805 (7th Cir. 2001), citing *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984).

162 29 Am. Jur. Proof of Facts 3rd, § 9.1 (2004).

163 *Smith v. Van Gorkom,* 488 A.2d 858, 872 (Del. 1985), citing *Zapata Corp. v. Maldonado,* 430 A.2d 779, 782 (Del. 1981).

164 *See* 18B Am. Jur. 2d Corporations, § 1703 (2004); *Eldridge v. Tymshare, Inc*. 186 Cal. App. 3d 767 (6th Dist. 1986).

165 *In re Caremark,* 698 A.2d 959, 967 (Del. Ch. 1996).

166 *Smith v. Van Gorkom,* 488 A.2d 858, 872 (Del. 1985).

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the director has availed himself or herself of all material information reasonably available to the director prior to making the decision.[167] A director's duty to become informed, and the director's ability to derive the protections provided by the Business Judgment Rule, arises from the fiduciary duty owed by the director to the corporation and its shareholders.[168]

1. Application of the Business Judgment Rule

The Business Judgment Rule is a doctrine created by courts, not by statutes, and thus the courts govern its application. As discussed below, developing case law establishes that corporate directors and officers must not only investigate reports of alleged wrongdoing, but must also ensure that systems are in place to monitor potential misconduct in the workplace. Electing not to conduct an internal investigation when confronted with a government investigation may subject the corporation to avoidable risks of shareholder actions, potential increased criminal penalties, and liability for failing to conduct investigations when called for by the circumstances.

In 1996, a Delaware Court of Chancery decided the landmark case of *In re Caremark, Inc.*[169] *Caremark* recognized a duty on the part of directors to monitor an organization's compliance with legal obligations.[170] In *Caremark*, a healthcare corporation pled guilty to the federal offense of mail fraud and agreed to pay civil and criminal fines totaling approximately $250 million.[171] Thereafter, its shareholders sued Caremark's directors, alleging that they had breached their fiduciary duties by failing to supervise corporate employees adequately, thereby exposing the corporation to criminal liability and penalties.

In approving a settlement of the shareholders' suit, the court explained "that absent grounds to suspect deception, neither corporate boards nor senior officers can be charged with wrongdoing simply for assuming the integrity of employees and the honesty of their dealings on the company's behalf."[172] However, the court emphasized, directors must "exercise a good faith judgment that the corporation's information and reporting system are in concept and design adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations." Moreover, it cautioned, failure to attempt to ensure an adequate reporting system "may, in theory at least, render a director liable for losses caused by noncompliance with applicable standards."[173] The court determined that when personal liability is alleged based upon ignorance of the underlying activities that caused the loss to the corporation, "only a sustained or systematic failure of the board to exercise oversight—such as an utter failure to attempt to assure a reasonable information and reporting system exists—will establish the lack of good faith that is a necessary condition to liability."[174]

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167 *Id.*

168 *Lutz v. Boas*, 171 A.2d 381 (Del. Ch. 1961)

169 698 A.2d 959 (Del. Ch. 1996).

170 Sarah Helene Duggin, *Internal Corporate Investigations: Legal Ethics, Professionalism, and the Employee Interview*, Colum. Bus. L. Rev. 859, 882 (2003).

171 *Caremark*, 698 A.2d at 960-61.

172 *Id.* at 969.

173 *Id.* at 970.

174 *Id.* at 971

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The issue highlighted in *Caremark* has resurfaced in several subsequent federal decisions. In *McCall v. Scott,*[175] for example, the Court held that, under appropriate circumstances, directors might be liable civilly for reckless acts or omissions by a corporation's agents. In particular, *McCall* involved a plaintiff's allegations that corporate directors should be held liable because of their failure to act, either intentionally or in reckless disregard of red flags that warned of systematic fraudulent practices employed and encouraged by management.

In contrast, when directors rely in good faith upon a corporate decision-making process, the elements of the process are critical in establishing good faith, and ultimately in avoiding unwarranted civil liability.[176] The key is that directors must ensure that an adequate information gathering-and-reporting process is in place.

2. Insulating Officers and Directors Under the Business Judgment Rule

There are a number of ways a corporation can position its officers and directors to be protected under the Business Judgment Rule, while implementing sound corporate policies that will protect the corporation.

- First, a corporation must ensure that it has an adequate reporting system in place whereby employees and supervisors can make confidential reports regarding allegations of misconduct.

  A confidential reporting system will enable employees, historically the primary reporters of workplace misconduct, to feel secure that their complaints about misconduct will be addressed in a manner that does not jeopardize their positions. Having an adequate reporting system in place will assist in ensuring that the directors will have timely information available so that they may act appropriately upon that information. While "whistle blowers" are protected from retaliation under the Sarbanes-Oxley Act of 2002, as well as many state statutes, not all employees may be aware of this protection or they may not care to rely upon it, and will feel most comfortable knowing the corporation has a confidential reporting policy in effect.

- Second, the corporation must immediately assess the nature of the investigation and err on the side of caution in determining whether an investigation is warranted. If an investigation is warranted, the company must ensure that it is conducted by an experienced individual.

  By immediately assessing and initiating an investigation if appropriate, as well as responding to the results of the investigation, a corporation can demonstrate that it has an adequate mechanism in place for investigating, reporting and acting upon allegations of misconduct. However, because the Business Judgment Rule only applies to "informed" decisions, corporations must be careful to ensure that the investigation is conducted by competent, experienced counsel capable of performing a careful and diligent investigation and providing thorough legal advice.

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[175] *McCall v. Scott,* 239 F.3d 808 (6th Cir. 2001).

[176] *Dellastatious v. Williams*, 242 F.3d 191, 196 (4th Cir. 2001).

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- Third, a corporation should consider establishing a sub-committee of the board to address the government investigation and underlying allegations of misconduct and to oversee the process of the investigation.

  Such a sub-committee is particularly important when various board members might be contacted and interviewed about the misconduct allegations. A separate sub-committee also will enable the corporation to be free from suggestion that potentially conflicted board members influenced the investigation.

- Fourth, the corporation should establish a corporate compliance program that details the legal and ethical codes of conduct required of employees, managers and senior management at the corporation.

  A corporate compliance program should articulate the responsibility of employees to avoid participating in misconduct and their obligations to report incidents they witness in the workplace. Additionally, the compliance program should include adequate training of all employees in order to attempt to minimize potential adverse activity, as well as ensuring that all employees are aware of the process by which they can raise concerns.

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V. Responding to the Investigation

A. Determining the Basis of the Investigation

In order to effectively respond to a governmental investigation, initiate any potentially necessary remedial measures and properly defend itself, a corporation will need to immediately ascertain the purpose, scope and extent of the government's investigation. As a practical matter, information is power. Without appropriate levels of information, it is improbable that a corporation can adequately address the multitude of legal issues confronted in the course of a government investigation. Thus, it benefits the corporation to determine why it is being investigated, who is investigating it, the reasons for the investigation, if the investigation is legitimate, who is putting the corporation at risk and what actions should be taken in response.

Further, as it relates to corporate fiduciary responsibilities, the corporation needs to determine how substantial the problem is and what the corporation can do to resolve it. A speedy response to criminal conduct in the workplace is not only important to corporate stability, but it ultimately may aid the corporation if criminal charges are initiated. Under the United States Sentencing Guidelines, Section 8C2.5, when a corporation is ultimately charged with a criminal offense, the corporation's "Involvement in or Tolerance of Criminal Activity," "Effective Program to Prevent and Detect Violations of Law" and "Self-Reporting, Cooperation and Acceptance of Responsibility" are all factors that can influence the penalty.

Often, the documents sought via a search warrant or subpoena will provide an indication of the timeframe, events and individuals being investigated. Also, the questions asked by an agent during his or her interviews of employees working for the corporation will provide insight into the investigative intent and theory.

B. Determining Requirements and Responsibilities

As discussed above, the execution of a search warrant will often disrupt a corporation's everyday business. Investigators are likely to seize work papers, files and computers containing information regarding all financial activity, including, accounts receivable, accounts payable and inventory. This seizure, however, does not negate a corporation's responsibility to its employees or its customers. Thus, a corporation should have a backup system for all documents necessary to operate its business. This duplication also will allow a business to operate in the event of other interruptions, such as computer viruses, fires, intentional or negligent employee action, and the like.

A corporation must ensure that none of its employees take any actions to impede or obstruct the government's investigation. Any such activity subjects the individual, as well as the corporation, to potential criminal penalties.

If a subpoena is served upon a corporation, it should immediately be read in its entirety to determine: (1) the nature of the inquiry; (2) the specific items sought; (3) the issuing court; (4) the time requirements to respond; (5) who caused the issuance of the subpoena; and (6) the requirements necessary to respond.

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1. Indemnification

Generally, corporations have a duty to indemnify their directors, officers and employees for civil, administrative and criminal liabilities incurred arising from their employment. Indemnification may be granted by statute, common law or corporation by-laws. Additionally, most corporations insure against this obligation through the use of Directors and Officers (D & O) insurance.

Indemnification generally includes expenses, including attorneys' fees, judgments, fines and amounts paid in settlement actually and reasonably incurred by the person in connection with the legal action.[177] Often, there are certain requirements that must first be met by the individual seeking indemnification. For example, the individual must demonstrate that he or she acted in good faith and in a manner that he or she reasonably believed to be in or not opposed to the best interests of the corporation.[178] Also, with respect to any criminal action or proceeding, the person must have no reasonable cause to believe that his conduct was unlawful.[179]

Often, the individual will request the advancement of legal expenses. Generally, an undertaking letter should be signed which allows for the repayment of the legal expenses if it is later determined that the individual is not entitled to those expenses.[180]

As a practical matter, even if the corporation is not required by statute or its by-laws to indemnify an employee, it may want to consider doing so. The failure to indemnify its employees, even if legally correct, is often a very bad tactical decision by the corporation. During government investigations, disgruntled employees can be very problematic. Accordingly, it is often cheaper in the long run to pay the legal expenses of the employees, enter into a joint defense agreement with them and put the corporation in a stronger, unified position.

C. Determining the Team to Respond

The basis of the investigation will determine the composition of the response team.

1. Attorneys

Attorneys should always be included in the response team, as their legal expertise is needed to evaluate facts and apply the necessary law to those facts. Attorneys will be able to determine the obligations, responsibilities and requirements of a corporation under investigation and make recommendations concerning how to appropriately and thoroughly respond to the government's investigatory requests. The corporation should utilize counsel that is experienced in responding to

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177 See Del. Code Ann. Section 145(a).

178 *Id.*

179 *Id.*

180 Del. Code Ann. § 145 (e) ("Expenses (including attorneys' fees) incurred by an officer or director in defending any civil, criminal, administrative or investigative action, suit or proceeding may be paid by the corporation in advance of the final disposition of such action, suit or proceeding upon receipt of an undertaking by or on behalf of such director or officer to repay such amount if it shall ultimately be determined that such person is not entitled to be indemnified by the corporation as authorized in this section. Such expenses (including attorneys' fees) incurred by former directors and officers or other employees and agents may be so paid upon such terms and conditions, if any, as the corporation deems appropriate.").

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government investigations. In selecting who should oversee this response, the corporation should consider:

- Counsel's experience of the counsel in conducting and responding to investigations;
- The availability of additional resources that may be necessary;
- The familiarity of counsel in the applicable laws and the law of corporate responsibility;
- Independence; and
- The familiarity of counsel with the government agencies and their personnel involved in the investigation.

2. Experienced Investigators

Experienced investigators are also extremely useful when responding to a government investigation due to their past history in conducting these investigations and their familiarity with the techniques utilized by the agencies. Additionally, their expertise in conducting interviews and amassing information will be beneficial in gathering the necessary level of knowledge to determine what actions are in the corporation's best interests. Retired federal and state investigators have a wealth of experience in determining facts that are crucial to the investigation, and are skilled in identifying how to independently corroborate those facts and evaluating the facts in light of the relevant law. Further, as they likely have investigated similar cases while employed by the government, these investigators assist greatly in analyzing the purpose and meaning behind the documents sought and the questions asked by the investigating agents.

3. Forensic Accountants

If the investigation includes allegations of financial fraud, a financial or forensic accounting expert should be retained to review and analyze the documents that have been subpoenaed or seized by the agents in the course of their investigation. This analysis always should be done with a view towards litigation and under the guidance and request of counsel to insulate this review under applicable privileges.

4. Electronic Evidence Collection Expert

Depending upon the scope of government's investigation, a corporation may need to retain an electronic evidence collection expert. It has become a routine investigative technique to subpoena corporate documents. Based upon the number of employees and the scope of the request, this may be a logistical challenge, involving imaging large numbers of computers and vast quantities of documents. An electronic evidence collection expert can assist a corporation in retrieving, searching, and organizing large volumes of documents in response to subpoenas and in enabling the corporation to conduct its own search and analysis.

Consideration must be given to utilizing an outside electronic data expert. The corporate information systems department may not always be qualified to gather and retrieve all of the information sought, and any problems with the production will be viewed negatively by the government agency if they were caused by an internal corporate department. Additionally, the perception of the credibility of the production by the governmental agency is likely to be better if performed by an outside expert.

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D. Practical Considerations

The appropriate considerations in responding to any governmental investigation depend upon the nature of the inquiry, its seriousness, and the potential consequences. However, the need to take any investigative process very seriously can't be over-emphasized. Failure to appropriately consider the consequences can have a devastating effect. The following factors should be considered when determining the appropriate responses:

- When first confronted with an investigation, learn as much as possible about: (1) the agency conducting the investigation; (2) its responsibilities; (3) the individual investigators; and (4) the usual methods utilized in such an investigation;
- Determine whether experienced counsel should be retained;
- Decide whether to conduct an internal investigation to learn more about the nature of the underlying allegations;
- Ensure that the appropriate persons within the corporation are involved in the process from the beginning;
- Determine what, if any, legal requirements are necessary for responding to the investigation;
- Develop and/or implement a coordinated media response plan;
- Determine whether there are any mandatory reporting requirements;
- Determine who will oversee the day-to-day corporate status of the government's investigation;
- Determine who will oversee any required or voluntary response to the investigation;
- Plan for additional investigative measures to be undertaken;
- Ensure that there is a proper reporting and update process in place within the corporation so that senior management will be adequately informed;
- Ensure that any document responses are coordinated through counsel so that privilege issues can be adequately protected;
- Ensure that document responses are adequately organized so that any necessary tracking can be accomplished. (This usually requires that a Bates numbering system be employed);
- Ensure that employees are properly informed;
- Review and update any contact information for key personnel;
- Determine if any employee has been interviewed and appropriately debrief that employee;
- Properly prepare any employee who has been subpoenaed to testify, including determining if he needs separate counsel;
- Consider whether a spoliation letter should be sent to employees informing them that no relevant documents should be destroyed; and
- Do not underestimate the seriousness of any governmental investigation.

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VI. Corporate Privileges

In any government investigation, a corporation's privileges are extremely important. The ability of the corporation to create appropriate privileges and maintain those privileges must be considered at each stage of the investigation. Without adequate attention to this subject at all times, the corporation or its employees may inadvertently waive the privilege as it applies to documents, discussions, communications and defense strategies. The privileges that will be discussed in this section include the: (1) attorney-client; (2) work-product; (3) self evaluative; and (4) joint defense privileges.

A. Attorney-Client Privilege

The purpose of the attorney-client privilege "is to encourage clients to make a full disclosure to their attorneys."[181] Federal courts generally recognize that the attorney-client privilege applies if:

> (1) The asserted holder of the privilege is or sought to become a client;
> (2) the person to whom the communication was made (a) is a member of the bar of a court, or his subordinate and (b) in connection with this communication is acting as a lawyer;
> (3) the communication relates to a fact of which the attorney was informed (a) by his client (b) without the presence of strangers (c) for the purpose of securing primarily either (i) an opinion on law or (ii) legal services or (iii) assistance in some legal proceeding, and not (d) for purpose of committing a crime or tort; and
> (4) the privilege has been (a) claimed and (b) not waived by the client.[182]

1. Corporate Counsel and Corporate Employees

While the attorney-client privilege applies to corporations as well as individuals, privileged communications in a corporate setting often involve a number of different employees and not just one single individual or entity that conveys privileged information. Case law has developed to define the privilege in the corporate context. Specifically, corporate communications are privileged if:

> (1) The communication is made for the purpose of securing legal advice,
> (2) the employee making the communication does so at the request of a corporate superior,
> (3) the superior requests the communication so that the corporation can secure legal advice,
> (4) the subject matter of the communication is within the scope of the employee's corporate duties, and
> (5) the communication is not disseminated beyond those persons who, because of the corporate structure, need to know its contents.[183]

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[181] *Fisher v. United States*, 425 U.S. 391, 403 (1976) (citation omitted).

[182] *See* Earl Silbert, *The Erosion of the Attorney-Client Privilege and Work Product Doctrine in Federal Criminal Investigations*, American College of Trial Lawyers (2002).

[183] *See Upjohn v. United States*, 449 U.S. 383 (1981).

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Communications that merely transmit facts may be discoverable because the privilege most commonly applies to requests for legal advice. However, when factual recitations result from "an implied request for legal advice," communications of fact information are privileged.[184] This privilege was created in order to protect information related to seeking legal advice. Thus, where a lawyer's role does not involve providing legal advice, privilege claims may be rejected.[185]

2. Corporate Counsel and Former Employees

Questions concerning the validity of the attorney-client privilege often arise when dealing with former employees. Several courts have upheld the privilege even though the communications involved former corporate employees.[186] However, not all courts have applied the privilege with respect to former employees.[187] Thus, counsel will need to evaluate the need for communications with former employees during the scope of any corporate investigation into allegations raised by a government investigation. As former employees do not generally have a duty to cooperate with the corporation– absent some other severance or consulting agreement– the potential for the corporation to obtain the former employee's cooperation often is limited by the personal relationships and friendships formed while the employee was employed.

3. Corporate Counsel and Consultants

Several courts have also upheld the privilege when an attorney utilizes the services of and communicates with a third-party consultant. To preserve the privilege in this situation, it is generally necessary that the consultant "improve the comprehension of the communications between attorney and client"[188] and that the communications with the consultant "be made in confidence for the purpose of obtaining legal advice from the lawyer."[189] Thus, communications to an accountant merely to obtain accounting advice, in contrast to facilitating legal advice, will not be privileged.[190] That being said, some jurisdictions have also recognized that if a consultant is the "functional equivalent" of an employee, communications may remain privileged.[191]

Corporations should be careful when consulting a media-relations consultant to assist the corporation with responding to the government's investigation. Unless great care is taken, any discussions with this consultant likely will be discoverable.[192] In *F.T.C. v. GlaxoSmithKline*,[193] the Federal Trade Commission sought to enforce an administrative subpoena request for documents. Reversing the district court, the Court of Appeals for the District of Columbia Circuit, held that the documents share by GlaxoSmithKline (GSK) with its public relations firm were protected by the attorney client privilege. The court found it persuasive that the corporate counsel "worked with these consultants in the same manner as they d[id] with full-time employees; indeed, the consultants

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184 *In re Pfizer Inc. Securities Litigation*, 1993 WL 561125 *6 (S.D.N.Y. Dec. 23, 1993).
185 *See*, e.g., *United States v. Chen,* 99 F.3d 1495 (9th Cir. 1996).
186 *See, e.g., In re Allen*, 106 F.3d 582, 605 (4th Cir. 1997).
187 *See Clark Equip. Co. v. Lifts Parts Mfg. Co.,* 1985 WL 2917 (N.D. Ill. Oct. 1, 1985).
188 *United States v. Ackert*, 169 F.3d 136, 139-140 (2nd Cir. 1999).
189 *United States v. Kovel,* 296 F.2d 918, 922 (2nd Cir. 1961).
190 *Id.*
191 *In re Copper Market Antitrust Litigation*, 200 F.R.D. 213, 217-19 (S.D.N.Y. 2001).
192 *See, Dorf & Stanton Communications Inc., v. Molson Breweries*, 100 F.3d 919 (Fed. Cir. 1996). [Editor's Note: Please check court.]
193 *F.T.C. v. GlaxoSmithKline*, 294 F.3d 141 (D.C. Cir. 2002).

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acted as part of a team with full-time employees regarding their particular assignments" and, as a result, the consultants "became integral members of the team assigned to deal with issues [that] ... were completely intertwined with [GSK's] litigation and legal strategies."[194] While this case is illustrative of methods that should be employed in an attempt to protect such communications, courts have not unilaterally adopted this approach, and thus this issue requires vigilance.

B. Work Product Doctrine

The work product doctrine protects documents and other tangible things that were prepared in anticipation of litigation or for trial from discovery by another party, unless the party seeking disclosure demonstrates "substantial need" and "undue hardship."[195] The work product immunity reaches a far greater number of documents and communications than the attorney-client privilege.[196] Provided that materials are prepared in anticipation of litigation, the work product doctrine may cover matters involving non-attorneys as well as lawyers.[197]

In order to reap the benefit of the work product doctrine, the documents must be obtained or prepared in anticipation of litigation.[198] Thus, documents prepared in the regular course of business fall outside the work product doctrine, even if litigation is imminent.[199] The same holds true for documents prepared to meet regulatory requirements.[200] However, recent cases indicate that documents that are prepared for dual purposes – legal advice and as a response to governmental investigation – may be protected from forced disclosure.[201] However, in no event can the other party obtain documents that contain the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of the party concerning litigation.[202] Further, while purely factual data is not ordinarily protected from discovery, where documents are assembled by or at a lawyer's direction in anticipation of litigation, discovery is precluded to prevent revealing the lawyer's thought process.[203]

C. Self Evaluative Privilege

Some courts have recognized a limited privilege that precludes discovery, on public-policy grounds, of internal, self-evaluative activities. To qualify for the privilege:

> [F]irst, the information must result from a critical self-analysis undertaken by the party seeking protection; second, the public must have a strong interest in preserving the free flow of the type of

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194 *Id.* at 148.

195 *See* Fed. R. Civ. P. 26(b)(3).

196 *See United States v. Nobles*, 422 U.S. 225, 238 n.11 (1975), citing *Hickman v. Taylor*, 329 U.S. 495, 508 (1947).

197 *Id.* at 238-39.

198 *Id.*

199 *See Bank Brussels Lambert v. Fiddler, Gonzales & Rodriguez*, 2003 WL 21277139 (S.D.N.Y. June 2, 2003), citing *Oxyn Telecommunications, Inc. v. Onse Telecom*, 2003 WL 660848 *4 n.4 (S.D.N.Y. 2003).

200 *See, e.g., National Union Fire Ins. Co. of Pittsburgh, Pa. v. Murray Sheet Metal Co., Inc.*, 967 F.2d 980, 984 (4th Cir. 1992).

201 *See, e.g., In re Grand Jury Subpoena*, 350 F.3d 1010 (9th Cir. 2003); *In re Grand Jury Subpoena*, 357 F.3d 900 (9th Cir. 2000).

202 *See Hickman v. Taylor*, 329 U.S. 495, 510-11 (1947).

203 *Sporck v. Peil*, 759 F.2d 312, 316 (3rd Cir. 1985).

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> information sought; and finally, the information must be of the type whose flow would be curtailed if discovery were allowed.[204]

However, the Supreme Court has recognized that "privileges are not lightly created nor expansively construed, for they are in derogation of the search for truth."[205] Thus, the majority of federal courts have refused to recognize the self evaluative privilege when presented in any context, especially when the information sought is factual information as opposed to analytical or evaluative information.[206] To date, all courts have refused to recognize the privilege when documents subject to a claim of the self evaluative privilege are sought by a government agency.[207] Accordingly, should documents fitting within this subject area be requested via formal process, production will be required in most cases.

D. Joint Defense Agreement Privilege

Joint defense agreements have become a very common tool in the defense of multiple parties during all stages of government investigations. The joint defense privilege arose initially as an extension of the attorney-client privilege against disclosure of confidential communications.[208] An intrusion by the government into an attorney-client relationship may be deemed a violation of a defendant's Sixth Amendment right to effective assistance of counsel or Fifth Amendment due process rights[209]– even if the intrusion is unintentional.[210]

Ordinarily, the attorney-client privilege will be deemed waived where a client discloses the contents of an otherwise privileged communication to a third party or where the communication occurs in the presence of third parties.[211] However, the joint defense privilege was created as an exception to this rule, whereby communications between a client and his personal lawyer would remain protected by the attorney-client privilege if they were disclosed to co-defendants or their counsel for the purpose of preparing a common defense.[212] The joint defense privilege may be asserted when: (1) the communications were made in the course of a joint defense effort; (2) the statements were designed to further that effort; and (3) the privilege has not been otherwise waived.[213] One party to a joint defense agreement generally cannot waive the privilege.

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[204] *In re Grand Jury Proceedings*, 861 F. Supp. 386, 388 (D. Md. 1994) citing Note, *The Privilege of Self Critical Analysis*, 96 Harv. L. Rev. 1083, 1086 (1983).

[205] *United States v. Nixon*, 418 U.S. 683, 710 (1974).

[206] Alan M. Klinger & James L. Bernard, *An Update to a Comprehensive Survey of the Attorney-Client Privilege and Work Product Doctrine by Honorable Alvin K. Hellerstein*, SJ035 ALI-ABA 801, 808-12 (2003).

[207] *See In re Kaiser Aluminum & Chem Co.*, 214 F.3d 586, 593 (5th Cir. 2000); *F.T.C. v. TRW, Inc.,* 628 F.2d 207, 210 (D.C. Cir. 1980); *In re Grand Jury Proceedings*, 861 F. Supp. 386 (D. Md. 1994).

[208] *United States v. Stepney*, 246 F. Supp. 2d 1069, 1074 (N.D. Cal. 2003).

[209] *United States v. Haynes*, 216 F.3d 789, 796 (9th Cir. 2000).

[210] *United States v. Aulicino*, 44 F.3d 1102, 1117 (2nd Cir. 1995).

[211] *See, e.g., Painewebber Group, Inc. v. Zinsmeyer Trusts Partnership*, 187 F.3d 988 (8th Cir. 1999)(attorney-client privilege); *Burton v. R.J. Reynolds Tobacco Co.*, 170 F.R.D. 481, 485 (D.Kan. 1997)(work product); *Diversified Industries, Inc. v. Meredith*, 572 F.2d 596 (8th Cir. 1978).

[212] *Hundyee v. United States*, 355 F.2d 183, 185 (9th Cir. 1965); *United States v. Stepney*, 246 F. Supp 2d. 1069, 1075 (N.D. Cal. 2003).

[213] *See, e.g. United States v. Weissman*, 195 F.3d 96, 99 (2nd Cir. 1999); *United States v. Evans*, 113 F.3d 1457,1467 (7th Cir. 1997).

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No written agreement is required to invoke the joint defense privilege. However, the existence of a written agreement does establish that parties are collaborating, thus guarding against a possible finding that a particular communication was made spontaneously rather than pursuant to a joint defense effort.[214] A written joint defense agreement also protects against misunderstandings among the parties and varying accounts of what was agreed to by the various attorneys and their clients. At least one federal court has ordered, post indictment, that joint defense agreements be in writing and filed with the court for its *in camera* review.[215] The court's review was conducted *in camera* in order to preclude the government from gaining any advantage by learning potential trial strategies of the defense. This review was premised on the court's supervisory authority to inquire into the "precise nature of a criminal defendant's representation to ensure that no conflict of interest exists that would deprive a defendant of his Sixth Amendment right to effective assistance of counsel."[216]

Federal Rules of Criminal Procedure 44(e) addresses this potential for conflict of interest. This rule requires a court to address multiple representation situations which may be triggered based on the joint defense agreement. This may present problems when the language of the joint defense agreement requires a duty of loyalty and confidentiality between a lawyer and all defendants who participate in the agreement.[217] Accordingly, care should be taken when entering a joint defense agreement to insure that the language clearly establishes that the duty of each counsel is to his individual client.[218]

The benefit of joint defense agreements is that they allow, but do not require, the sharing of otherwise privileged material to further the interests of multiple parties whose interests are parallel. In order to provide effective representation, often counsel will conclude, from time to time, that the interests of their respective clients will be best served by sharing documents, factual material, mental impressions, strategies, legal theories, memoranda, interview reports, and other information, including confidences of each client. In the absence of such sharing under a joint defense agreement, these materials would be privileged from disclosure to adverse or other parties as a result of the attorney-client privilege, the attorney work product privilege and other applicable privileges. Thus, the purpose of the joint defense agreement is to ensure that the exchange and disclosure of these otherwise protected materials do not diminish in any fashion the confidentiality of the materials and do not constitute a waiver of any privilege.[219]

When a government agency initiates an investigation into corporate entities, it is likely to seek interviews with current or former employees. Having separate counsel represent the employees of the corporation is a common practice. This practice eliminates conflicts that occur when corporate counsel also represents an employee, who later develops antagonistic interests with the corporation. By entering into a joint defense with separate counsel, the corporation gains the benefit of information from the employee without the attendant risk of conflicts.

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214 *United States v. Weissman,* 195 F.3d 96, 98- 99 (2d Cir.1999).

215 *United States v. Stepney*, 246 F. Supp. 2d 1069 (N.D. Cal. 2003).

216 *Id.* at 1077.

217 *Id.* at 1079.

218 For example, "Counsel have advised their respective Clients that they are represented only by their own attorney in this matter, and that while the attorneys representing the other Client parties to the Agreement have a duty to preserve the confidences disclosed to them pursuant to the Agreement, each attorney will be acting only as the attorney for their respective Client and will owe a duty of loyalty only to their own Client."

219 A sample Joint Defense Agreement is enclosed with this InfoPAK.

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E. Disclosure

A corporation should always conduct itself in response to a government investigation with an eye towards maintaining privileges. There may come a time where the corporation elects to waive its privileges, and to disclose its privileged information to government agencies or other third parties. There are also occasions where the privileges can be inadvertently waived.

1. Deliberate Disclosure

Generally, a party waives its ability to assert either the attorney-client privilege or work product protection by voluntarily disclosing privileged documents to a third party.[220] Under the majority view, disclosure of privileged communications results in a waiver of all other communications regarding the same subject matter.[221]

a. Limited Waiver

A minority of courts have recognized the existence of a limited waiver of privilege when a voluntary disclosure is made to a governmental agency.[222] Additionally, in areas where a limited waiver is recognized, corporations should seek a written agreement from the Department of Justice or other government agency before turning over privileged material. The ability to engage in a limited waiver, however, is not guaranteed. Indeed, some courts have permitted third party discovery notwithstanding written limited-waiver agreements between holders of the privileges and the Government.[223] A number of courts have refused to recognize the existence of a limited waiver despite confidentiality agreements with the Department of Justice and the SEC.[224] These courts have dismissed the viability of a "limited waiver" and have found that a corporation which discloses work-product protected documents to the SEC, whether pursuant to a confidentiality agreement or not, has waived the work product privilege in a subsequent action by the shareholders of the company because the corporation was adversarial to the SEC at the time of the disclosure.[225] Thus, while a company may be able to mitigate potential SEC proceedings by providing information to the SEC, there is no guarantee that the disclosed information will remain privileged from discovery and use by third parties in subsequent civil litigation.

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220 *See, e.g., Painewebber Group, Inc. v. Zinsmeyer Trusts Partnership*, 187 F.3d 988 (8th Cir. 1999)(attorney-client privilege); *Burton v. R.J. Reynolds Tobacco Co.*, 170 F.R.D. 481, 485 (D.Kan. 1997)(work product); *Diversified Industries, Inc. v. Meredith*, 572 F.2d 596 (8th Cir. 1978).

221 *See, e.g., In re Grand Jury Proceedings,* 219 F.3d 175 (2nd Cir. 2000*); Texaco Puerto Rico, Inc. v. Dept. of Consumer Affairs*, 60 F.3d 867, 883 (1st Cir. 1995).

222 *See, e.g., Byrnes v. IDS Realty Trust*, 85 F.R.D. 679, 688 (S.D.N.Y. 1980); *In Diversified Industries, Inc. v. Meredith*, 572 F.2d 596, 611 (8th Cir. 1978)(*en banc*).

223 *See, e.g., Permian Corp. v. United States*, 665 F.2d 1214, 1219-21 (D.D.C. 1981).[Editor's Note: Please check court..D.C. Cir?.]

224 *McKesson HBOC, Inc. v. Superior Court of San Francisco Cty*., 9 Cal. Rptr. 3d 812, 819-21 (Cal. App. 1st Dist. 2004); *McKesson Corp. v. Green*, 597 S.E. 2d 447, 454 (Ga. App.2004); *Westinghouse Elec. Corp. v. Republic of Philippines*, 951 F.2d 1414, 1427 (3rd Cir. 1991).

225 *McKesson HBOC, Inc. v. Superior Court of San Francisco Cty*., 9 Cal. Rptr. 3d 812, 820-21 (Cal. App. 1st Dist. 2004).

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2. Inadvertent Disclosure

The general rules governing waiver of a privilege become more complicated when the issue arises in the context of corporate entities. Corporations communicate with their lawyers only through their agents. Similarly, a corporation cannot directly waive the privilege when disclosure is in its best interest because individuals must accomplish the waiver on behalf of the corporation.[226] If a corporation disseminates information to the public that reveals parts of privileged communications or which rely on privileged reports, the privilege may be deemed waived.[227]

In In re Grand Jury Proceedings v. John Doe,[228] the corporation had not expressly waived its privilege but the government alleged that a corporate officer impliedly waived the privilege during his grand jury testimony. This presents a common and challenging situation, where the corporate officer is questioned, under oath, without the benefit of counsel at his side. Originally, the district court found that a waiver had occurred. The Second Circuit held that a corporate officer can impliedly waive a corporation's attorney-client and work-product privileges in the officer's grand jury testimony, even though the corporation explicitly refused such a waiver. However, in this particular case, the court determined that based on the limited record before it, "it would be unfair to find, on the basis of Witness's testimony, that Doe Corp. had waived its entitlement to preserve the confidentiality of its communications with its attorneys."[229] The court held that the implied waiver analysis should be guided primarily by fairness principles. The factors to be used to determine the scope of that waiver include: (1) the relationship of the individual to the corporation; (2) the grand jury context; (3) the nature of the disclosure; and (4) the prejudice to the government. Ultimately, upon remand,[230] the district court determined that the first three factors weighed heavily in favor of finding that a wavier had occurred. However, because the district court also determined that the government had alternative methods of obtaining necessary information, it found that there was no waiver.

However, there are several cases that have held that the testimony of a corporate officer, even in contravention of corporate instructions, does constitute a waiver of the corporation's privilege.[231] Accordingly, extreme care must be exercised at all times regarding the privileged nature of corporate materials and information, the results of any internal investigation, the identity of those with access to that privileged material, and their activities of these individuals as they might affect that privilege. Accordingly, the use of experienced counsel in these matters is crucial to advise all parties regarding the potential consequences attendant with governmental investigatory techniques.

3. Mandatory Disclosure

Absent a specific government directive, there is no legal obligation to report crimes, let alone misconduct which may not rise to the level of criminal activity. Not even the offense of misprision of felony criminalizes non-reporting, because that crime requires active concealment rather than a

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226 *In re Grand Jury Proceedings v. John Doe*, 219 F.3d 175, 183 (2nd Cir. 2000), citing *Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 348 (1985).

227 *Id.* at 184.

228 *In re Grand Jury Proceedings v. John Doe*, 219 F.3d 175 (2nd Cir. 2000).

229 *Id.* at 190.

230 2001 WL 237377 (S.D.N.Y. DATE? 2001).

231 *Velsicol Chemical Corp. v. Parsons*, 561 F.2d 671, 675 (7th Cir. 1977); *Weil v. Investment/Indicators, Research and Management, Inc.*, 647 F.2d 18, 23-25 (9th Cir. 1981).

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mere failure to report. However, there are several limited areas of the law that do impose an affirmative duty to report crimes. These obligations generally are limited to highly regulated industries. For instance, a bank is required to file a "Suspicious Activity Report" if it detects "known or suspected" criminal violations committed or attempted against the bank or through the bank.[232] There are also obligations stemming from the anti-fraud provisions of the federal securities laws and SEC, NYSE, AMEX and NASDAQ provisions that may require disclosure in public filings and proxy statements.[233] Additionally, when certain hazardous materials are released, federal law mandates reports.[234]In the health care field, for example, failure to return funds improperly obtained mandates affirmative action.[235]

4. Crime-Fraud Exception to Privileges

The proponent of a privilege may be precluded from successfully asserting attorney-client privilege or work product protection. For example "attorney-client communications lose their privileged character when the attorney is consulted 'to further a continuing or contemplated criminal or fraudulent scheme.'"[236] The crime-fraud exception applies only where the crime or fraud was contemplated by the client at the time counsel was consulted.[237] The crime-fraud exception does not reach disclosures of past wrongdoing, which ordinarily remain shielded by the attorney-client privilege.[238] To overcome the attorney-client privilege, the proponent of the crime-fraud exception must make a *prima facie* showing that the legal advice in question was obtained in furtherance of illegal or fraudulent activity.[239]

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232 *See* 12 C.F.R. § 563.180, 353, and 21.11 (requiring that a Suspicious Activity Reports be filed by banks).

233 *See* 15 U.S.C. § 77-78.

234 42 U.S.C. § 9603.

235 42 U.S.C. § 1320a-7b.

236 *Pritchard-Keang Nam Corp. v. Jaworski*, 751 F.2d 277, 281 (8th Cir. 1984), *quoting In re Berkley & Co.*, 629 F.2d 548, 553 (8th Cir. 1980) (citations omitted).

237 *See, e.g., SEC v. Herman*, 2004 WL 964104 (S.D.N.Y. May 5, 2004).

238 *See, e.g., United States v. Zolin,* 491 U.S. 554 (1989).

239 *United States v. Weingold*, 2003 WL 21702280 (3rd Cir. DATE? 2003).

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VII. Additional Resources

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Beth A. Wilkerson & Steven H. Schulman, When Talk is Not Cheap: Communication with the Media, the Government and Other Parties in High Profile White Collar Criminal Cases, 39 Am. Crim. L. Rev. 203 (2002).

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Dennis J. Block & Simon C. Roosevelt, *Responding To A Corporate Crisis*, 1249 P.L.I./Corp. 531 (2001)Thomas M. DiBiagio, *Federal Criminal Law and the Crime-Fraud Exception: Disclosure of Privileged Conversations and Documents Should Not Be Compelled Without the Government's Factual Foundation Being tested by the Crucible of Meaningful Adversarial Testing*, 62 Md. L. Rev. 1 , 2003.

Ralph C. Ferrara, et al., *Shareholder Derivative Litigation: Besieging the Board,* § 10.05 (2001).

Michael J. Holland, *Footing the Bill: Paying the Legal Costs of Criminal Proceedings*, 69 DEF. COUNS. J. 27 (2002).

Barbara L. Johnson, *Tactical and Ethical Considerations in Investigations of Employment Related Matters*, American Law Institute - American Bar Association Continuing Legal Education July 25-27, 2002 Current Developments in Employment Law, SH014 ALI-ABA 729.

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John F. Savarese & Carol Miller, *Protecting Privilege and Dealing Fairly With Employees While Conducting an Internal Investigation, in CRISIS MANAGEMENT & BUSINESS RECOVERY: ARE YOU PREPARED*? 2002, 1296 PLI/CORP. 63 (PLI Order No. B0-01HQ, 2002).

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David N. Zornow & Keith D. Krakaur, *On the Brink of a Brave New World: The Death of Privilege in Corporate Criminal Investigations*, 37 AM. CRIM. L. REV. 147 (2000).

John K. Villa, *The Opening Moves of the SEC Investigation*, ACCA 2003 Annual Meeting Materials, pg. 34, available at: http://www.acca.com/education03/am/cm/608.pdf (analyzing whether to use outside or in-house counsel in an SEC investigation on the basis of skill, conflict of interest).

In re Grand Jury Proceedings, 219 F.3d 175, 190-91 (2d Cir. 2000) (discusses the test to be used when corporate officers are found to have waived the corporation's attorney-client and work-product privileges in grand jury testimony even though the corporation explicitly refused to waive these privileges).

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VIII. Relevant Materials

A. Sample Joint Defense Agreement

B. Thompson Memorandum

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ATTORNEY-CLIENT PRIVILEGED
JOINT DEFENSE AGREEMENT

I. BACKGROUND

This Agreement, by and among the undersigned counsel and their clients ("parties"), memorializes the understandings reached among them regarding the common defense of any and all civil, administrative, and criminal investigations relating to potential violations by *names of corporate entities and individuals who are participating in the joint defense agreement* or any other employee or former employee by the *List the Investigating Agencies* or other governmental agencies.

This Agreement also confirms that to the extent counsel have already been in communication with one another, those communications have been subject to the oral joint defense agreement, which this document memorializes.

II. MUTUALITY OF INTEREST

The undersigned believe that there are common questions of law and fact and that there is a mutuality of interest in a common and joint defense of their clients in regard to the above-referenced matters, and any related civil, criminal or administrative proceedings. Accordingly, the parties wish to continue to pursue their separate but common interests, and avoid any suggestion of waiver of the confidentiality of privileged communications, memoranda and documents. Counsel believe participation in this agreement is necessary to effectuate the best possible representation on behalf of their respective clients. The undersigned intend and understand that communications among them are privileged and protected from disclosure to any third party by the attorney-client, and the attorney work product privileges, and other applicable privileges.

In order to provide effective representation, the undersigned counsel have concluded that, from time to time, the interests of our respective clients will be best served by sharing documents, factual material, mental impressions, strategies, legal theories, memoranda, interview reports, and other information, including confidences of each client, all of which will hereinafter be referred to as "Joint Defense Materials." In the absence of such sharing, these Joint Defense Materials would be privileged from disclosure to adverse or other parties as a result of the attorney-client privilege, the attorney work product privilege and other applicable privileges. It is the purpose of the Agreement to ensure that the exchange and disclosure of Joint Defense Material contemplated herein do not diminish in any fashion the confidentiality of the Joint Defense Materials and do not constitute a waiver of any privilege otherwise applicable.

III. MAINTENANCE OF PRIVILEGE

Any written information that is shared or exchanged pursuant to this agreement shall be marked "PRIVILEGED AND CONFIDENTIAL–SUBJECT TO JOINT DEFENSE AGREEMENT" or the equivalent, provided however, that inadvertent failure to so mark such information shall not be deemed a waiver of any applicable privilege. Communications and exchanges of documents among the parties shall be deemed Joint Defense Materials and shall remain as fully protected by the attorney-client, work product and other privileges as though the exchange or communication had not occurred. The Joint Defense Materials are exchanged by the parties only in the interest of facilitating the potential joint defense of the matters under investigation. But for their expectation that the communications and documents will remain privileged, no exchange of Joint Defense Materials would take place.

The parties agree that they will not produce the contents of any communications made or document received under this Agreement to any person, corporation, counsel, entity or government agency or official, other than to their clients or to legal counsel or others assisting in providing representation, without the written consent of all parties to this Agreement.

It is further understood and agreed that any Joint Defense Material shall be used solely in connection with the investigation, and any related civil, criminal or administrative proceedings.

This Agreement does not restrict any of the parties from using or disclosing information or materials that do not contain any privileged information covered by this Agreement. It is expressly understood that nothing contained herein shall limit the right of any counsel to disclose any such documents or information obtained from such counsel. The parties recognize their right to conduct separate witness interviews or otherwise to undertake independent investigative efforts. Any party undertaking such separate investigative efforts may disclose these separate investigative efforts to any third parties or to use the information in any manner which that party desires, without the consent of any other party to the Agreement. Furthermore, any information already in the possession of a party is not made subject to the Agreement by the subsequent receipt of the same information from another party to this Agreement.

The parties to this Agreement are free to use any leads and to make derivative use of any privileged information, including information that was obtained from any party that subsequently withdraws from the Agreement. Such derivative information may be used for any purpose, including cross-examination of any party or former party to this Agreement.

IV. DEMAND OR SUBPOENA OF MATERIAL

If any other person or entity requests or demands, by subpoena or otherwise, any Joint Defense Materials, counsel will immediately notify all parties to afford them the opportunity to seek protection from the compelled disclosure of the information.

V. JOINT DEFENSE DOCTRINE

It is the parties' intention and understanding that (a) the existence of this Agreement, (b) the fact that particular communications have been made between and among parties to this Agreement, (c) the information communicated and documents shared under the protection of this Agreement, and (d) any part of memoranda or other work product containing or referring to such communications and documents, shall remain confidential and protected from disclosure to any third party by each Client's "attorney-client privilege," each Client's "attorney work product doctrine," the "common interest privilege," and the "joint defense doctrine," as recognized in such cases as *United States v. Stepney*, 246 F. Supp. 2d 1069 (N.D. CA. 2003); *In Re Sealed Case*, 29 F.3d 715, 718 (D.C. Cir. 1994); *Continental Oil Company v. United States*, 330 F.2d 347 (9th Cir. 1964); *Hunydee v. United States*, 355 F.2d 183 (9th Cir. 1965); *In the Matter of a Grand Jury Subpoena, Dated November 16, 1974*, 406 F. Supp. 381 (S.D.N.Y. 1975); and *United States v. McPartlin*, 595 F.2d 1321 (7th Cir. 1979).

Unless required by court order or other compulsion of law or as may be necessary to protect privileged communications from compelled disclosure, no party to this Joint Defense Agreement will reveal the existence, nature or extent of this Agreement to any third party including, but not limited to, any governmental authority.

VI. WITHDRAWAL AND NOTIFICATION

In the event any party decides to withdraw from this Agreement for any reason (including but not limited to the entry by a Client into an agreement, formal or informal, with any law enforcement agency or governmental department for cooperation, immunity, non-prosecution or plea agreement) their counsel shall immediately notify the undersigned counsel, in writing, of their withdrawal from the Agreement, which will thereupon be terminated as to that Client, provided, however, that no such termination shall affect or impair the obligations of confidentiality with respect to Joint Defense Materials previously furnished pursuant to the Agreement. Further, any party shall, upon withdrawal, return all materials provided by other parties hereto, including any copies of Joint Defense Materials that the party has in their possession or made.

The parties to this Agreement warrant that none of them, as of the date of the execution of this Agreement has commenced negotiations to cooperate with or obtain immunity from the government. If any party to this Agreement is immunized or becomes a cooperating witness for the government or commences negotiations toward any such event, counsel for such party shall

provide immediate written notice to each of the parties to this Agreement. It is understood and agreed that any party to this Agreement is free to cooperate with the government, and the fact of such cooperation does not necessarily mean that the parties no longer have common interests.

VII. CONFLICT OF INTEREST AND DISQUALIFICATION

Each Client understands that it is possible that another party or parties to the Agreement may later become adverse witnesses or otherwise hold an adverse position. Each Client understands that counsel for the other clients may advise their Clients to cooperate with the government, generate and/or disclose evidence or information to the government or to third parties, and/or may examine the Client at trial or another proceeding. The undersigned counsel have considered these factors and believe that advantages of being a party to this Agreement outweigh any of the potential disadvantages posed by this Agreement. Therefore, as a condition precedent to the receipt of any Joint Defense Material or information, the parties agree that they will not assert any future claim that any attorney to this Agreement is disqualified or otherwise barred from continuing his or her representation in this matter by virtue of his or her receipt of information of Joint Defense Material.

Counsel and their respective Clients hereto further agree that in the event that any such Client becomes a cooperating government witness, nothing in the Agreement shall create a conflict of interest so as to require the disqualification of any counsel from the representation of their respective Client, and the parties hereby waive any such conflict of interest. The parties further agree that neither the Joint Defense Materials received from each other, nor the contents thereof, will be used to cross-examine any such Client who, either as a cooperating government witness or in any other capacity, becomes a witness at any proceeding. However, derivative information may be used for any purpose, including cross-examination.

It is further agreed that no attorney who has entered into the Agreement shall be disqualified from examining or cross-examining any party to the Agreement who testifies at any proceeding, whether under a grant of immunity or otherwise, because of such attorney's participation in the Agreement.

Counsel and their respective Clients hereto further agree that any conflict of interest, actual or perceived, rising out of this Joint Defense Agreement is hereby waived. Each Client hereby knowingly and intelligently waives any conflict of interest that may arise from an attorney member of the Agreement, other than their own attorney, examining them at any proceeding.

VIII. SCOPE OF REPRESENTATION

Counsel have advised their respective Clients that they are represented only by their own attorney in this matter, and that while the attorneys representing the other Client parties to the Agreement have a duty to preserve the confidences disclosed to them pursuant to the Agreement, each attorney will be acting only as the attorney for their respective Client and will owe a duty of

loyalty only to their own Client.

This Agreement does not create any agency or similar relationship among the parties to it. No party to this Agreement shall have the authority to waive any applicable privilege or claim on behalf of any other party to the Agreement. Nor shall any waiver of any applicable privilege or claim by the conduct of any party be construed to apply to any other party to the Agreement.

IX. INJUNCTIVE RELIEF

The parties acknowledge that disclosure of any communication in violation of the Agreement will cause the parties to suffer irreparable harm for which there is no adequate legal remedy. Each party acknowledges that immediate injunctive relief is an appropriate and necessary remedy for any violation or threatened violation of this Agreement.

The parties further agree that any unauthorized disclosures in violation of the Agreement shall not serve as or constitute a waiver of privilege.

X. CONTINUATION OF AGREEMENT

The Agreement shall continue in effect notwithstanding any conclusion or resolution as to any party hereto of the investigation or any pending or future administrative, civil or criminal proceedings arising from or relating to it. The parties will continue to be bound by the Agreement following such conclusion or resolution.

XI. EXECUTION AND MODIFICATION

By signing the Agreement each attorney certifies that he or she has explained the contents of this Joint Defense Agreement to his or her Client, and that the Client understands and agrees to abide by the understandings reflected in the Agreement. Any modifications of the agreement must be in writing and signed by all parties. Other parties may be permitted to join this Agreement provided that all existing parties to the Agreement are notified and consent.

This Agreement may be signed in any number of counterparts.

THE FOREGOING IS AGREED TO by the following parties through their counsel.

Dated:

LAW FIRM

By:_____

_____, Esq.

Attorney for _____

Dated:

LAW FIRM

By:_____
_____, Esq.
Attorney for _____

Dated:

LAW FIRM

By:_____
_____, Esq.
Attorney for _____

161 Federal Prosecution of Business Organizations -- DAG Letter

The Deputy Attorney General

Washington, D.C. 20530

January 20, 2003

MEMORANDUM

TO: Heads of Department Components
United States Attorneys

FROM: Larry D. Thompson
Deputy Attorney General

SUBJECT:Principles of Federal Prosecution of Business Organizations

As the Corporate Fraud Task Force has advanced in its mission, we have confronted certain issues in the principles for the federal prosecution of business organizations that require revision in order to enhance our efforts against corporate fraud. While it will be a minority of cases in which a corporation or partnership is itself subjected to criminal charges, prosecutors and investigators in every matter involving business crimes must assess the merits of seeking the conviction of the business entity itself.

Attached to this memorandum are a revised set of principles to guide Department prosecutors as they make the decision whether to seek charges against a business organization. These revisions draw heavily on the combined efforts of the Corporate Fraud Task Force and the Attorney General's Advisory Committee to put the results of more than three years of experience with the principles into practice.

The main focus of the revisions is increased emphasis on and scrutiny of the authenticity of a corporation's cooperation. Too often business organizations, while purporting to cooperate with a Department investigation, in fact take steps to impede the quick and effective exposure of the complete scope of wrongdoing under investigation. The revisions make clear that such conduct should weigh in favor of a corporate prosecution. The revisions also address the efficacy of the corporate governance mechanisms in place within a corporation, to ensure that these measures are truly effective rather than mere paper programs.

Further experience with these principles may lead to additional adjustments. I look forward to hearing comments about their operation in practice. Please forward any comments to Christopher Wray, the Principal Associate Deputy Attorney General, or to Andrew Hruska, my Senior Counsel.

162 Federal Prosecution of Business Organizations

Federal Prosecution of Business Organizations[1]

I. Charging a Corporation: General

A. General Principle: Corporations should not be treated leniently because of their artificial nature nor should they be subject to harsher treatment. Vigorous enforcement of the criminal laws against corporate wrongdoers, where appropriate results in great benefits for law enforcement and the public, particularly in the area of white collar crime. Indicting corporations for wrongdoing enables the government to address and be a force for positive change of corporate culture, alter corporate behavior, and prevent, discover, and punish white collar crime.

B. Comment: In all cases involving corporate wrongdoing, prosecutors should consider the factors discussed herein. First and foremost, prosecutors should be aware of the important public benefits that may flow from indicting a corporation in appropriate cases. For instance, corporations are likely to take immediate remedial steps when one is indicted for criminal conduct that is pervasive throughout a particular industry, and thus an indictment often provides a unique opportunity for deterrence on a massive scale. In addition, a corporate indictment may result in specific deterrence by changing the culture of the indicted corporation and the behavior of its employees. Finally, certain crimes that carry with them a substantial risk of great public harm, e.g., environmental crimes or financial frauds, are by their nature most likely to be committed by businesses, and there may, therefore, be a substantial federal interest in indicting the corporation.

Charging a corporation, however, does not mean that individual directors, officers, employees, or shareholders should not also be charged. Prosecution of a corporation is not a substitute for the prosecution of criminally culpable individuals within or without the corporation. Because a corporation can act only through individuals, imposition of individual criminal liability may provide the strongest deterrent against future corporate wrongdoing. Only rarely should provable individual culpability not be pursued, even in the face of offers of corporate guilty pleas.

Corporations are "legal persons," capable of suing and being sued, and capable of committing crimes. Under the doctrine of *respondeat superior*, a corporation may be held criminally liable for the illegal acts of its directors, officers, employees, and agents. To hold a corporation liable for these actions, the government must establish that the corporate agent's actions (i) were within the scope of his duties and (ii) were intended, at least in part, to benefit the corporation. In all cases involving wrongdoing by corporate agents, prosecutors should consider the corporation, as well as the responsible individuals, as potential criminal targets.

Agents, however, may act for mixed reasons -- both for self-aggrandizement (both direct and indirect) and for the benefit of the corporation, and a corporation may be held liable as long as one motivation of its agent is to benefit the corporation. In *United States v. Automated Medical Laboratories*, 770 F.2d 399 (4th Cir. 1985), the court affirmed the corporation's conviction for the actions of a subsidiary's employee despite its claim that the employee was acting for his own benefit, namely his "ambitious nature and his desire to ascend the corporate ladder." The court stated, "*Partucci* was clearly acting in part to benefit AML since his advancement within the corporation depended on AML's well-being and its lack of difficulties with the FDA." Similarly, in *United States v. Cincotta*, 689 F.2d 238, 241-42 (1st Cir. 1982), the court held, "criminal liability may be imposed on the corporation only where the agent is acting within the scope of his employment. That, in turn, requires that the agent be performing acts of the kind which he is authorized to perform, and those acts must be motivated -- at least in part -- by an intent to benefit the corporation." Applying this test, the court upheld the corporation's

conviction, notwithstanding the substantial personal benefit reaped by its miscreant agents, because the fraudulent scheme required money to pass through the corporation's treasury and the fraudulently obtained goods were resold to the corporation's customers in the corporation's name. As the court concluded, "Mystic--not the individual defendants--was making money by selling oil that it had not paid for."

Moreover, the corporation need not even necessarily profit from its agent's actions for it to be held liable. In *Automated Medical Laboratories*, the Fourth Circuit stated:

> [B]enefit is not a "touchstone of criminal corporate liability; benefit at best is an evidential, not an operative, fact." Thus, whether the agent's actions ultimately redounded to the benefit of the corporation is less significant than whether the agent acted with the intent to benefit the corporation. The basic purpose of requiring that an agent have acted with the intent to benefit the corporation, however, is to insulate the corporation from criminal liability for actions of its agents which be inimical to the interests of the corporation or which may have been undertaken solely to advance the interests of that agent or of a party other than the corporation.

770 F.2d at 407 (emphasis added; quoting *Old Monastery Co. v. United States*, 147 F.2d 905, 908 (4th Cir.), cert. denied, 326 U.S. 734 (1945)).

II. Charging a Corporation: Factors to Be Considered

A. General Principle: Generally, prosecutors should apply the same factors in determining whether to charge a corporation as they do with respect to individuals. *See* USAM § 9-27.220, *et seq.* Thus, the prosecutor should weigh all of the factors normally considered in the sound exercise of prosecutorial judgment: the sufficiency of the evidence; the likelihood of success at trial,; the probable deterrent, rehabilitative, and other consequences of conviction; and the adequacy of noncriminal approaches. *See* id. However, due to the nature of the corporate "person," some additional factors are present. In conducting an investigation, determining whether to bring charges, and negotiating plea agreements, prosecutors should consider the following factors in reaching a decision as to the proper treatment of a corporate target:

1. the nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of corporations for particular categories of crime (*see* section III, *infra*);

2. the pervasiveness of wrongdoing within the corporation, including the complicity in, or condonation of, the wrongdoing by corporate management (*see* section IV, *infra*);

3. the corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it (*see* section V, *infra*);

4. the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, including, if necessary, the waiver of corporate attorney-client and work product protection (*see* section VI, *infra*);

5. the existence and adequacy of the corporation's compliance program (*see* section VII, *infra*);

6. the corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies (*see* section VIII, *infra*);

7. collateral consequences, including disproportionate harm to shareholders, pension holders and employees not proven personally culpable and impact on the public arising from the prosecution (*see*

section IX, *infra*); and

8. the adequacy of the prosecution of individuals responsible for the corporation's malfeasance;

9. the adequacy of remedies such as civil or regulatory enforcement actions (*see section X, infra*).

B. Comment: As with the factors relevant to charging natural persons, the foregoing factors are intended to provide guidance rather than to mandate a particular result. The factors listed in this section are intended to be illustrative of those that should be considered and not a complete or exhaustive list. Some or all of these factors may or may not apply to specific cases, and in some cases one factor may override all others. The nature and seriousness of the offense may be such as to warrant prosecution regardless of the other factors. Further, national law enforcement policies in various enforcement areas may require that more or less weight be given to certain of these factors than to others.

In making a decision to charge a corporation, the prosecutor generally has wide latitude in determining when, whom, how, and even whether to prosecute for violations of Federal criminal law. In exercising that discretion, prosecutors should consider the following general statements of principles that summarize appropriate considerations to be weighed and desirable practices to be followed in discharging their prosecutorial responsibilities. In doing so, prosecutors should ensure that the general purposes of the criminal law -- assurance of warranted punishment, deterrence of further criminal conduct, protection of the public from dangerous and fraudulent conduct, rehabilitation of offenders, and restitution for victims and affected communities -- are adequately met, taking into account the special nature of the corporate "person."

III. Charging a Corporation: Special Policy Concerns

A. General Principle: The nature and seriousness of the crime, including the risk of harm to the public from the criminal conduct, are obviously primary factors in determining whether to charge a corporation. In addition, corporate conduct, particularly that of national and multi-national corporations, necessarily intersects with federal economic, taxation, and criminal law enforcement policies. In applying these principles, prosecutors must consider the practices and policies of the appropriate Division of the Department, and must comply with those policies to the extent required.

B. Comment: In determining whether to charge a corporation, prosecutors should take into account federal law enforcement priorities as discussed above. *See* USAM § 9-27-230. In addition, however, prosecutors must be aware of the specific policy goals and incentive programs established by the respective Divisions and regulatory agencies. Thus, whereas natural persons may be given incremental degrees of credit (ranging from immunity to lesser charges to sentencing considerations) for turning themselves in, making statements against their penal interest, and cooperating in the government's investigation of their own and others' wrongdoing, the same approach may not be appropriate in all circumstances with respect to corporations. As an example, it is entirely proper in many investigations for a prosecutor to consider the corporation's pre-indictment conduct, *e.g.*,voluntary disclosure, cooperation, remediation or restitution, in determining whether to seek an indictment. However, this would not necessarily be appropriate in an antitrust investigation, in which antitrust violations, by definition, go to the heart of the corporation's business and for which the Antitrust Division has therefore established a firm policy, understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government. As another example, the Tax Division has a strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses. Thus, in determining whether or not to charge a corporation, prosecutors should consult with the Criminal, Antitrust, Tax, and Environmental and Natural Resources Divisions, if appropriate or required.

IV. Charging a Corporation: Pervasiveness of Wrongdoing Within the Corporation

A. General Principle: A corporation can only act through natural persons, and it is therefore held responsible for

the acts of such persons fairly attributable to it. Charging a corporation for even minor misconduct may be appropriate where the wrongdoing was pervasive and was undertaken by a large number of employees or by all the employees in a particular role within the corporation, *e.g.*, salesmen or procurement officers, or was condoned by upper management. On the other hand, in certain limited circumstances, it may not be appropriate to impose liability upon a corporation, particularly one with a compliance program in place, under a strict *respondeat superior* theory for the single isolated act of a rogue employee. There is, of course, a wide spectrum between these two extremes, and a prosecutor should exercise sound discretion in evaluating the pervasiveness of wrongdoing within a corporation.

B. Comment: Of these factors, the most important is the role of management. Although acts of even low-level employees may result in criminal liability, a corporation is directed by its management and management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged. As stated in commentary to the Sentencing Guidelines:

> Pervasiveness [is] case specific and [will] depend on the number, and degree of responsibility, of individuals [with] substantial authority ... who participated in, condoned, or were willfully ignorant of the offense. Fewer individuals need to be involved for a finding of pervasiveness if those individuals exercised a relatively high degree of authority. Pervasiveness can occur either within an organization as a whole or within a unit of an organization.

USSG §8C2.5, comment. (n. 4).

V. Charging a Corporation: The Corporation's Past History

A. General Principle: Prosecutors may consider a corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it, in determining whether to bring criminal charges.

B. Comment: A corporation, like a natural person, is expected to learn from its mistakes. A history of similar conduct may be probative of a corporate culture that encouraged, or at least condoned, such conduct, regardless of any compliance programs. Criminal prosecution of a corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and yet it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the conduct in spite of the warnings or enforcement actions taken against it. In making this determination, the corporate structure itself, *e.g.*, subsidiaries or operating divisions, should be ignored, and enforcement actions taken against the corporation or any of its divisions, subsidiaries, and affiliates should be considered. *See* USSG § 8C2.5(c) & comment. (n. 6).

VI. Charging a Corporation: Cooperation and Voluntary Disclosure

A. General Principle: In determining whether to charge a corporation, that corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate with the government's investigation may be relevant factors. In gauging the extent of the corporation's cooperation, the prosecutor may consider the corporation's willingness to identify the culprits within the corporation, including senior executives; to make witnesses available; to disclose the complete results of its internal investigation; and to waive attorney-client and work product protection.

B. Comment: In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation itself. It will often be difficult to determine which individual took which action on behalf of the corporation. Lines of authority and responsibility may be shared among operating divisions or departments, and records and personnel may be spread throughout the United States or even among several countries. Where the criminal conduct continued over an extended period of time, the culpable or knowledgeable personnel may have been promoted, transferred, or fired, or they may have quit or retired. Accordingly, a corporation's cooperation may be critical in identifying the culprits and locating

relevant evidence.

In some circumstances, therefore, granting a corporation immunity or amnesty or pretrial diversion may be considered in the course of the government's investigation. In such circumstances, prosecutors should refer to the principles governing non-prosecution agreements generally. *See* USAM § 9-27.600-650. These principles permit a non prosecution agreement in exchange for cooperation when a corporation's "timely cooperation appears to be necessary to the public interest and other means of obtaining the desired cooperation are unavailable or would not be effective." Prosecutors should note that in the case of national or multi-national corporations, multi-district or global agreements may be necessary. Such agreements may only be entered into with the approval of each affected district or the appropriate Department official. *See* USAM §9-27.641.

In addition, the Department, in conjunction with regulatory agencies and other executive branch departments, encourages corporations, as part of their compliance programs, to conduct internal investigations and to disclose their findings to the appropriate authorities. Some agencies, such as the SEC and the EPA, as well as the Department's Environmental and Natural Resources Division, have formal voluntary disclosure programs in which self-reporting, coupled with remediation and additional criteria, may qualify the corporation for amnesty or reduced sanctions.[2] Even in the absence of a formal program, prosecutors may consider a corporation's timely and voluntary disclosure in evaluating the adequacy of the corporation's compliance program and its management's commitment to the compliance program. However, prosecution and economic policies specific to the industry or statute may require prosecution notwithstanding a corporation's willingness to cooperate. For example, the Antitrust Division offers amnesty only to the first corporation to agree to cooperate. This creates a strong incentive for corporations participating in anti-competitive conduct to be the first to cooperate. In addition, amnesty, immunity, or reduced sanctions may not be appropriate where the corporation's business is permeated with fraud or other crimes.

One factor the prosecutor may weigh in assessing the adequacy of a corporation's cooperation is the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protections, both with respect to its internal investigation and with respect to communications between specific officers, directors and employees and counsel. Such waivers permit the government to obtain statements of possible witnesses, subjects, and targets, without having to negotiate individual cooperation or immunity agreements. In addition, they are often critical in enabling the government to evaluate the completeness of a corporation's voluntary disclosure and cooperation. Prosecutors may, therefore, request a waiver in appropriate circumstances.[3] The Department does not, however, consider waiver of a corporation's attorney-client and work product protection an absolute requirement, and prosecutors should consider the willingness of a corporation to waive such protection when necessary to provide timely and complete information as one factor in evaluating the corporation's cooperation.

Another factor to be weighed by the prosecutor is whether the corporation appears to be protecting its culpable employees and agents. Thus, while cases will differ depending on the circumstances, a corporation's promise of support to culpable employees and agents, either through the advancing of attorneys fees,[4] through retaining the employees without sanction for their misconduct, or through providing information to the employees about the government's investigation pursuant to a joint defense agreement, may be considered by the prosecutor in weighing the extent and value of a corporation's cooperation. By the same token, the prosecutor should be wary of attempts to shield corporate officers and employees from liability by a willingness of the corporation to plead guilty.

Another factor to be weighed by the prosecutor is whether the corporation, while purporting to cooperate, has engaged in conduct that impedes the investigation (whether or not rising to the level of criminal obstruction). Examples of such conduct include: overly broad assertions of corporate representation of employees or former employees; inappropriate directions to employees or their counsel, such as directions not to cooperate openly and fully with the investigation including, for example, the direction to decline to be interviewed; making presentations or submissions that contain misleading assertions or omissions; incomplete or delayed production of records; and failure to promptly disclose illegal conduct known to the corporation.

Finally, a corporation's offer of cooperation does not automatically entitle it to immunity from prosecution. A corporation should not be able to escape liability merely by offering up its directors, officers, employees, or agents as in lieu of its own prosecution. Thus, a corporation's willingness to cooperate is merely one relevant factor, that needs to be considered in conjunction with the other factors, particularly those relating to the corporation's past history and the role of management in the wrongdoing.

VII. Charging a Corporation: Corporate Compliance Programs

A. General Principle: Compliance programs are established by corporate management to prevent and to detect misconduct and to ensure that corporate activities are conducted in accordance with all applicable criminal and civil laws, regulations, and rules. The Department encourages such corporate self-policing, including voluntary disclosures to the government of any problems that a corporation discovers on its own. However, the existence of a compliance program is not sufficient, in and of itself, to justify not charging a corporation for criminal conduct undertaken by its officers, directors, employees, or agents. Indeed, the commission of such crimes in the face of a compliance program may suggest that the corporate management is not adequately enforcing its program. In addition, the nature of some crimes, *e.g.*, antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program.

B. Comment: A corporate compliance program, even one specifically prohibiting the very conduct in question, does not absolve the corporation from criminal liability under the doctrine of *respondeat superior. See United States v. Basic Construction Co.*, 711 F.2d 570 (4th Cir. 1983) ("a corporation may be held criminally responsible for antitrust violations committed by its employees if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if... such acts were against corporate policy or express instructions."). In *United States v. Hilton Hotels Corp.*, 467 F.2d 1000 (9th Cir. 1972), *cert. denied*, 409 U.S. 1125 (1973), the Ninth Circuit affirmed antitrust liability based upon a purchasing agent for a single hotel threatening a single supplier with a boycott unless it paid dues to a local marketing association, even though the agent's actions were contrary to corporate policy and directly against express instructions from his superiors. The court reasoned that Congress, in enacting the Sherman Antitrust Act, "intended to impose liability upon business entities for the acts of those to whom they choose to delegate the conduct of their affairs, thus stimulating a maximum effort by owners and managers to assure adherence by such agents to the requirements of the Act."[5] It concluded that "general policy statements" and even direct instructions from the agent's superiors were not sufficient; "Appellant could not gain exculpation by issuing general instructions without undertaking to enforce those instructions by means commensurate with the obvious risks." *See also United States v. Beusch,* 596 F.2d 871, 878 (9th Cir. 1979) ("[A] corporation may be liable for the acts of its employees done contrary to express instructions and policies, but ... the existence of such instructions and policies may be considered in determining whether the employee in fact acted to benefit the corporation."); *United States v. American Radiator & Standard Sanitary Corp.*, 433 F.2d 174 (3rd Cir. 1970) (affirming conviction of corporation based upon its officer's participation in price-fixing scheme, despite corporation's defense that officer's conduct violated its "rigid anti-fraternization policy" against any socialization (and exchange of price information) with its competitors; "When the act of the agent is within the scope of his employment or his apparent authority, the corporation is held legally responsible for it, although what he did may be contrary to his actual instructions and may be unlawful.").

While the Department recognizes that no compliance program can ever prevent all criminal activity by a corporation's employees, the critical factors in evaluating any program are whether the program is adequately designed for maximum effectiveness in preventing and detecting wrongdoing by employees and whether corporate management is enforcing the program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve business objectives. The Department has no formal guidelines for corporate compliance programs. The fundamental questions any prosecutor should ask are: "Is the corporation's compliance program well designed?" and "Does the corporation's compliance program work?" In answering these questions, the prosecutor should consider the comprehensiveness of the compliance program; the extent and pervasiveness of

the criminal conduct; the number and level of the corporate employees involved; the seriousness, duration, and frequency of the misconduct; and any remedial actions taken by the corporation, including restitution, disciplinary action, and revisions to corporate compliance programs.[6] Prosecutors should also consider the promptness of any disclosure of wrongdoing to the government and the corporation's cooperation in the government's investigation. In evaluating compliance programs, prosecutors may consider whether the corporation has established corporate governance mechanisms that can effectively detect and prevent misconduct. For example, do the corporation's directors exercise independent review over proposed corporate actions rather than unquestioningly ratifying officers' recommendations; are the directors provided with information sufficient to enable the exercise of independent judgment, are internal audit functions conducted at a level sufficient to ensure their independence and accuracy and have the directors established an information and reporting system in the organization reasonable designed to provide management and the board of directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the organization's compliance with the law. *In re: Caremark,* 698 A.2d 959 (Del. Ct. Chan. 1996).

Prosecutors should therefore attempt to determine whether a corporation's compliance program is merely a "paper program" or whether it was designed and implemented in an effective manner. In addition, prosecutors should determine whether the corporation has provided for a staff sufficient to audit, document, analyze, and utilize the results of the corporation's compliance efforts. In addition, prosecutors should determine whether the corporation's employees are adequately informed about the compliance program and are convinced of the corporation's commitment to it. This will enable the prosecutor to make an informed decision as to whether the corporation has adopted and implemented a truly effective compliance program that, when consistent with other federal law enforcement policies, may result in a decision to charge only the corporation's employees and agents.

Compliance programs should be designed to detect the particular types of misconduct most likely to occur in a particular corporation's line of business. Many corporations operate in complex regulatory environments outside the normal experience of criminal prosecutors. Accordingly, prosecutors should consult with relevant federal and state agencies with the expertise to evaluate the adequacy of a program's design and implementation. For instance, state and federal banking, insurance, and medical boards, the Department of Defense, the Department of Health and Human Services, the Environmental Protection Agency, and the Securities and Exchange Commission have considerable experience with compliance programs and can be very helpful to a prosecutor in evaluating such programs. In addition, the Fraud Section of the Criminal Division, the Commercial Litigation Branch of the Civil Division, and the Environmental Crimes Section of the Environment and Natural Resources Division can assist U.S. Attorneys' Offices in finding the appropriate agency office and in providing copies of compliance programs that were developed in previous cases.

VIII. Charging a Corporation: Restitution and Remediation

A. General Principle: Although neither a corporation nor an individual target may avoid prosecution merely by paying a sum of money, a prosecutor may consider the corporation's willingness to make restitution and steps already taken to do so. A prosecutor may also consider other remedial actions, such as implementing an effective corporate compliance program, improving an existing compliance program, and disciplining wrongdoers, in determining whether to charge the corporation.

B. Comment: In determining whether or not a corporation should be prosecuted, a prosecutor may consider whether meaningful remedial measures have been taken, including employee discipline and full restitution.[7] A corporation's response to misconduct says much about its willingness to ensure that such misconduct does not recur. Thus, corporations that fully recognize the seriousness of their misconduct and accept responsibility for it should be taking steps to implement the personnel, operational, and organizational changes necessary to establish an awareness among employees that criminal conduct will not be tolerated. Among the factors prosecutors should consider and weigh are whether the corporation appropriately disciplined the wrongdoers and disclosed information concerning their illegal conduct to the government.

Employee discipline is a difficult task for many corporations because of the human element involved and sometimes because of the seniority of the employees concerned. While corporations need to be fair to their employees, they must also be unequivocally committed, at all levels of the corporation, to the highest standards of legal and ethical behavior. Effective internal discipline can be a powerful deterrent against improper behavior by a corporation's employees. In evaluating a corporation's response to wrongdoing, prosecutors may evaluate the willingness of the corporation to discipline culpable employees of all ranks and the adequacy of the discipline imposed. The prosecutor should be satisfied that the corporation's focus is on the integrity and credibility of its remedial and disciplinary measures rather than on the protection of the wrongdoers.

In addition to employee discipline, two other factors used in evaluating a corporation's remedial efforts are restitution and reform. As with natural persons, the decision whether or not to prosecute should not depend upon the target's ability to pay restitution. A corporation's efforts to pay restitution even in advance of any court order is, however, evidence of its "acceptance of responsibility" and, consistent with the practices and policies of the appropriate Division of the Department entrusted with enforcing specific criminal laws, may be considered in determining whether to bring criminal charges. Similarly, although the inadequacy of a corporate compliance program is a factor to consider when deciding whether to charge a corporation, that corporation's quick recognition of the flaws in the program and its efforts to improve the program are also factors to consider.

IX. Charging a Corporation: Collateral Consequences

A. General Principle: Prosecutors may consider the collateral consequences of a corporate criminal conviction in determining whether to charge the corporation with a criminal offense.

B. Comment: One of the factors in determining whether to charge a natural person or a corporation is whether the likely punishment is appropriate given the nature and seriousness of the crime. In the corporate context, prosecutors may take into account the possibly substantial consequences to a corporation's officers, directors, employees, and shareholders, many of whom may, depending on the size and nature (e.g., publicly vs. closely held) of the corporation and their role in its operations, have played no role in the criminal conduct, have been completely unaware of it, or have been wholly unable to prevent it. Prosecutors should also be aware of non-penal sanctions that may accompany a criminal charge, such as potential suspension or debarment from eligibility for government contracts or federal funded programs such as health care. Whether or not such non-penal sanctions are appropriate or required in a particular case is the responsibility of the relevant agency, a decision that will be made based on the applicable statutes, regulations, and policies.

Virtually every conviction of a corporation, like virtually every conviction of an individual, will have an impact on innocent third parties, and the mere existence of such an effect is not sufficient to preclude prosecution of the corporation. Therefore, in evaluating the severity of collateral consequences, various factors already discussed, such as the pervasiveness of the criminal conduct and the adequacy of the corporation's compliance programs, should be considered in determining the weight to be given to this factor. For instance, the balance may tip in favor of prosecuting corporations in situations where the scope of the misconduct in a case is widespread and sustained within a corporate division (or spread throughout pockets of the corporate organization). In such cases, the possible unfairness of visiting punishment for the corporation's crimes upon shareholders may be of much less concern where those shareholders have substantially profited, even unknowingly, from widespread or pervasive criminal activity. Similarly, where the top layers of the corporation's management or the shareholders of a closely-held corporation were engaged in or aware of the wrongdoing and the conduct at issue was accepted as a way of doing business for an extended period, debarment may be deemed not collateral, but a direct and entirely appropriate consequence of the corporation's wrongdoing.

The appropriateness of considering such collateral consequences and the weight to be given them may depend on the special policy concerns discussed in section III, *supra*.

X. Charging a Corporation: Non-Criminal Alternatives

A. General Principle: Although non-criminal alternatives to prosecution often exist, prosecutors may consider whether such sanctions would adequately deter, punish, and rehabilitate a corporation that has engaged in wrongful conduct. In evaluating the adequacy of non-criminal alternatives to prosecution, *e.g.*, civil or regulatory enforcement actions, the prosecutor may consider all relevant factors, including:

1. the sanctions available under the alternative means of disposition;

2. the likelihood that an effective sanction will be imposed; and

3. the effect of non-criminal disposition on Federal law enforcement interests.

B. Comment: The primary goals of criminal law are deterrence, punishment, and rehabilitation. Non-criminal sanctions may not be an appropriate response to an egregious violation, a pattern of wrongdoing, or a history of non-criminal sanctions without proper remediation. In other cases, however, these goals may be satisfied without the necessity of instituting criminal proceedings. In determining whether federal criminal charges are appropriate, the prosecutor should consider the same factors (modified appropriately for the regulatory context) considered when determining whether to leave prosecution of a natural person to another jurisdiction or to seek non-criminal alternatives to prosecution. These factors include: the strength of the regulatory authority's interest; the regulatory authority's ability and willingness to take effective enforcement action; the probable sanction if the regulatory authority's enforcement action is upheld; and the effect of a non-criminal disposition on Federal law enforcement interests. *See* USAM §§ 9-27.240, 9-27.250.

XI. Charging a Corporation: Selecting Charges

A. General Principle: Once a prosecutor has decided to charge a corporation, the prosecutor should charge, or should recommend that the grand jury charge, the most serious offense that is consistent with the nature of the defendant's conduct and that is likely to result in a sustainable conviction.

B. Comment: Once the decision to charge is made, the same rules as govern charging natural persons apply. These rules require "a faithful and honest application of the Sentencing Guidelines" and an "individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the Federal criminal code, and maximize the impact of Federal resources on crime." *See* USAM § 9-27.300. In making this determination, "it is appropriate that the attorney for the government consider, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." *See* Attorney General's Memorandum, dated October 12, 1993.

XII. Plea Agreements with Corporations

A. General Principle: In negotiating plea agreements with corporations, prosecutors should seek a plea to the most serious, readily provable offense charged. In addition, the terms of the plea agreement should contain appropriate provisions to ensure punishment, deterrence, rehabilitation, and compliance with the plea agreement in the corporate context. Although special circumstances may mandate a different conclusion, prosecutors generally should not agree to accept a corporate guilty plea in exchange for non-prosecution or dismissal of charges against individual officers and employees.

B. Comment: Prosecutors may enter into plea agreements with corporations for the same reasons and under the same constraints as apply to plea agreements with natural persons. *See* USAM §§ 9-27.400-500. This means, *inter alia*, that the corporation should be required to plead guilty to the most serious, readily provable offense charged. As is the case with individuals, the attorney making this determination should do so "on the basis of an individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the federal criminal code, and maximize the impact of federal resources on

crime. In making this determination, the attorney for the government considers, inter alia, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." *See* Attorney General's Memorandum, dated October 12, 1993. In addition, any negotiated departures from the Sentencing Guidelines must be justifiable under the Guidelines and must be disclosed to the sentencing court. A corporation should be made to realize that pleading guilty to criminal charges constitutes an admission of guilt and not merely a resolution of an inconvenient distraction from its business. As with natural persons, pleas should be structured so that the corporation may not later "proclaim lack of culpability or even complete innocence." *See* USAM §§ 9-27.420(b)(4), 9-27.440, 9-27.500. Thus, for instance, there should be placed upon the record a sufficient factual basis for the plea to prevent later corporate assertions of innocence.

A corporate plea agreement should also contain provisions that recognize the nature of the corporate "person" and ensure that the principles of punishment, deterrence, and rehabilitation are met. In the corporate context, punishment and deterrence are generally accomplished by substantial fines, mandatory restitution, and institution of appropriate compliance measures, including, if necessary, continued judicial oversight or the use of special masters. *See* USSG §§ 8B1.1, 8C2.1, *et seq*. In addition, where the corporation is a government contractor, permanent or temporary debarment may be appropriate. Where the corporation was engaged in government contracting fraud, a prosecutor may not negotiate away an agency's right to debar or to list the corporate defendant.

In negotiating a plea agreement, prosecutors should also consider the deterrent value of prosecutions of individuals within the corporation. Therefore, one factor that a prosecutor may consider in determining whether to enter into a plea agreement is whether the corporation is seeking immunity for its employees and officers or whether the corporation is willing to cooperate in the investigation of culpable individuals. Prosecutors should rarely negotiate away individual criminal liability in a corporate plea.

Rehabilitation, of course, requires that the corporation undertake to be law-abiding in the future. It is, therefore, appropriate to require the corporation, as a condition of probation, to implement a compliance program or to reform an existing one. As discussed above, prosecutors may consult with the appropriate state and federal agencies and components of the Justice Department to ensure that a proposed compliance program is adequate and meets industry standards and best practices. *See* section VII, *supra*.

In plea agreements in which the corporation agrees to cooperate, the prosecutor should ensure that the cooperation is complete and truthful. To do so, the prosecutor may request that the corporation waive attorney-client and work product protection, make employees and agents available for debriefing, disclose the results of its internal investigation, file appropriate certified financial statements, agree to governmental or third-party audits, and take whatever other steps are necessary to ensure that the full scope of the corporate wrongdoing is disclosed and that the responsible culprits are identified and, if appropriate, prosecuted. *See* generally section VIII, *supra.*

Footnotes:

1. While these guidelines refer to corporations, they apply to the consideration of the prosecution of all types of business organizations, including partnerships, sole proprietorships, government entities, and unincorporated associations.

2. In addition, the Sentencing Guidelines reward voluntary disclosure and cooperation with a reduction in the corporation's offense level. *See* USSG §8C2.5)g).

3. This waiver should ordinarily be limited to the factual internal investigation and any contemporaneous advice given to the corporation concerning the conduct at issue. Except in unusual circumstances, prosecutors should not seek a waiver with respect to communications and work product related to advice concerning the

government's criminal investigation.

4. Some states require corporations to pay the legal fees of officers under investigation prior to a formal determination of their guilt. Obviously, a corporation's compliance with governing law should not be considered a failure to cooperate.

5. Although this case and *Basic Construction* are both antitrust cases, their reasoning applies to other criminal violations. In the Hilton case, for instance, the Ninth Circuit noted that Sherman Act violations are commercial offenses "usually motivated by a desire to enhance profits," thus, bringing the case within the normal rule that a "purpose to benefit the corporation is necessary to bring the agent's acts within the scope of his employment." 467 F.2d at 1006 & n4. In addition, in *United States v. Automated Medical Laboratories*, 770 F.2d 399, 406 n.5 (4th Cir. 1985), the Fourth Circuit stated "that Basic Construction states a generally applicable rule on corporate criminal liability despite the fact that it addresses violations of the antitrust laws."

6. For a detailed review of these and other factors concerning corporate compliance programs, see United States Sentencing Commission, GUIDELINES MANUAL, §8A1.2, comment. (n.3(k)) (Nov. 1997). *See* also USSG §8C2.5(f)

7. For example, the Antitrust Division's amnesty policy requires that "[w]here possible, the corporation [make] restitution to injured parties...."

About the Firm

The matters handled by Lindquist & Vennum's White Collar and Regulatory Defense practice group include civil, administrative or regulatory matters before the Securities and Exchange Commission, National Association of Securities Dealers, the Food and Drug Administration, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, Office of Thrift Supervision, state licensure boards and the Department of Health and Human Services. Additionally, the group's practice includes shareholder derivative and class action matters, internal investigations, civil RICO (racketeering and corrupt organization) cases, and the representation of nonprofit institutions and their boards of directors.

The White Collar and Regulatory Defense practice group includes three former federal prosecutors all of whom have both prosecuted and defended economic crime cases. Prior experience includes substantial interaction with the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision, in both prosecuting and defending regulatory and enforcement initiatives. Lindquist & Vennum's White Collar and Regulatory Defense practice group also draws upon the talents and expertise of three former Securities and Exchange Commission attorneys, to include a former SEC Enforcement Division attorney, a former SEC senior counsel and a former SEC branch chief, and former members of the Minnesota Attorney General's Office with respect to both criminal and environmental law matters

The White Collar and Regulatory Defense practice group currently represents officers of publicly traded companies that are under investigation in securities fraud matters, which include parallel criminal and civil investigations by the Department of Justice and Securities and Exchange Commission, as well as filed shareholder litigation. Additionally the White Collar and Regulatory Defense practice group serves as counsel to individuals in arbitrations and mediations in securities matters, as well as counsel to companies and individuals in other insider trading, securities fraud investigations, and health care matters, whether internal, administrative, civil or criminal in nature, to include informal or formal Securities and Exchange Commission civil investigations. Lindquist & Vennum has experience in Truth-in-Lending and related compliance laws, and in representing clients faced with Section 1818 enforcement proceedings, including cease and desist orders, civil money penalties, removals, and Section 32 actions, while the White Collar and Regulatory Defense practice group lends expertise to Patriot Act, money laundering and mandatory disclosure laws.

Lindquist & Vennum current has approximate 170 lawyers, located both in Minneapolis and Denver. The firm's general practice is largely regional with certain national practices, including White Collar, Securities, Health Care and also internal investigations. Because of the expertise within the various practice groups, and this firm's internal policy of transcending practice groups to obtain the expertise necessary to each matter, Lindquist & Vennum combines a high sense of ethics with an unmatched level of expertise at a reasonable rate structure to provide the best value for the firm's clients.

About the writers

William Michael, Jr. spent more than a decade as a federal prosecutor, both in south Florida, as well as in Minnesota. During that time, Mr. Michael supervised a branch office of the United States Attorney's Office in the Southern District of Florida, investigated economic crimes, and coordinated health care fraud investigations and prosecutions on behalf of the United States Department of

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Justice. Mr. Michael has tried more than 100 jury trials, and routinely teaches nationwide to both investigators and lawyers in matters involving complex financial investigations and internal investigations. Mr. Michael now chairs the White Collar and Regulatory Defense practice group at Lindquist & Vennum. Mr. Michael represents health care providers in qui tam civil and criminal proceedings. Mr. Michael also represents corporations and conducts internal investigations on their behalf. Mr. Michael's clients include corporate senior management and executive personnel with respect to civil and criminal investigations conducted by federal and state authorities.

Mark D. Larsen also served for more than a decade as a federal prosecutor in both the Central District of California (Los Angeles) and the District of Minnesota. Mr. Larsen has been involved in both investigating and defending economic crime allegations involving public corruption, organized crime, insurance fraud, securities fraud, health care fraud, and the pharmaceutical industry. Mr. Larsen has tried more than 40 jury trials, has served as the Acting Chief of the Appellate Section of the United States Attorneys Office, and teaches advanced criminal law and procedure. Mr. Larsen represents corporations and individuals in the health care, agricultural and pharmaceutical industries.

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